DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT

24 CFR Parts 203 and 3500

[Docket No. FR–5180–P–01]

RIN 2502–AI61

Real Estate Settlement Procedures Act (RESPA): Proposed Rule To Simplify and Improve the Process of Obtaining Mortgages and Reduce Consumer Settlement Costs

AGENCY: Office of the Assistant Secretary for Housing—Federal Housing Commissioner, HUD.

ACTION: Proposed rule.

SUMMARY: This proposed rule presents HUD's proposal to simplify and improve the disclosure requirements for mortgage settlement costs under the Real Estate Settlement Procedures Act of 1974 (RESPA), to protect consumers from unnecessarily high settlement costs. This proposed rule takes into consideration: discussions during HUD's RESPA Reform Roundtables held in July and August 2005; public comments in response to HUD's July 29, 2002, proposed rule that addressed RESPA reform; and comments received and views expressed through congressional hearings; meetings with affected parties; and consultation with other federal agencies, including the Small Business Administration Office of Advocacy.

HUD's objective in proposing these revisions is to protect consumers from unnecessarily high settlement costs by taking steps to: Improve and standardize the Good Faith Estimate (GFE) form, to make it easier to use for shopping among settlement service providers; ensure that page one of the GFE provides a clear summary of the loan terms and total settlement charges so that borrowers will be able to use the GFE to comparison shop among loan originators for a mortgage loan; provide more accurate estimates of costs of settlement services shown on the GFE; improve disclosure of yield spread premiums to help borrowers understand how they can affect their settlement charges; facilitate comparison of the GFE and the HUD–1/HUD–1A Settlement Statements (HUD–1 settlement statement or HUD–1); ensure that at settlement borrowers are made aware of final loan terms and settlement costs, by reading and providing a copy of a ''closing script'' to borrowers; clarify HUD–1 instructions; clarify HUD's current regulations concerning discounts; and expressly state when RESPA permits certain pricing mechanisms that benefit consumers, including average cost pricing and discounts, including volume based discounts.

DATES: *Comment Due Date:* May 13, 2008.

ADDRESSES: Interested persons are invited to submit comments regarding this proposed rule. There are two methods for comments to be submitted as public comments and to be included in the public comment docket for this rule. Regardless of the method selected, all submissions must refer to the above docket number and title.

1. *Submission of Comments by Mail.* Comments may be submitted by mail to the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 Seventh Street, SW., Room 10276, Washington, DC 20410–0001.

2. *Electronic Submission of Comments.* Interested persons may submit comments electronically through the Federal eRulemaking Portal at *www.regulations.gov*. HUD strongly encourages commenters to submit comments electronically. Electronic submission of comments allows commenters maximum time to prepare and submit comments, ensures timely receipt by HUD, and enables HUD to make them immediately available to the public. Comments submitted electronically through the *www.regulations.gov* Web site can be viewed by other commenters and interested members of the public. Commenters should follow the instructions provided on that site to submit comments electronically.

Note: To receive consideration as public comments, comments must be submitted through one of the two methods specified above. Again, all submissions must refer to the docket number and title of the rule. No Facsimile Comments. Facsimile (FAX) comments are not acceptable.

Public Inspection of Public Comments. All properly submitted comments and communications submitted to HUD will be available, without charge, for public inspection and copying between 8 a.m. and 5 p.m. weekdays at the above address. Due to security measures at the HUD Headquarters building, an advance appointment to review the public comments must be scheduled by calling the Regulations Division at (202) 708–3055 (this is not a toll-free number). Individuals with speech or hearing impairments may access this number through TTY by calling the toll-free Federal Information Relay Service at (800) 877–8339. Copies of all comments submitted are available for inspection and downloading at *www.regulations.gov*.

FOR FURTHER INFORMATION CONTACT: Ivy Jackson, Director, or Barton Shapiro, Deputy Director, Office of RESPA and Interstate Land Sales, U.S. Department of Housing and Urban Development, 451 Seventh Street, SW., Room 9158, Washington, DC 20410; telephone number (202) 708–0502 (this is not a toll-free number). For legal questions, contact Paul S. Ceja, Assistant General Counsel for GSE/RESPA, Joan L. Kayagil, Deputy Assistant General Counsel for GSE/RESPA or Rhonda L. Daniels, Attorney-Advisor for GSE/RESPA, Room 9262; telephone number (202) 708–3137. Persons with hearing or speech impairments may access this number via TTY by calling the toll-free Federal Information Relay Service at (800) 877–8339. The address for the above listed persons is: Department of Housing and Urban Development, 451 Seventh Street, SW., Washington, DC 20410.

SUPPLEMENTARY INFORMATION:

I. Introduction and Principles

The process for disclosing settlement costs in the financing or refinancing of a home is regulated under RESPA, 12 U.S.C. 2601–2617. HUD seeks to make improvements to its regulations implementing RESPA (24 CFR part 3500), to make the process clearer and more useful and ultimately less costly for consumers. The mortgage industry has changed considerably since RESPA was enacted in 1974, and the regulations implementing RESPA's original disclosure requirements are no longer adequate.

The settlement costs associated with a mortgage loan are significant. In the case of purchase transactions, these costs can become an impediment to homeownership, particularly for low- and moderate-income households. HUD's current RESPA rules do not facilitate shopping or competition to lower these costs. HUD estimates that with the changes proposed to its RESPA regulations in this rulemaking, settlement costs will be lowered by $6.5 to $8.4 billion annually, with an average savings of $518 to $670 per transaction.

RESPA's purposes include the provision of effective advance disclosure of settlement costs and elimination of practices that tend to unnecessarily increase the costs of settlement services. Similarly, the Administration is committed to extending homeownership opportunities. HUD's regulatory reform and enforcement efforts for RESPA remain guided by the following principles:

1. Borrowers should receive loan terms and settlement cost information early enough in the process to allow them to shop for the mortgage product and settlement services that best meet their needs;

2. Costs should be disclosed and should be as firm as possible to avoid surprise charges at settlement;

3. Many of the current problems arise from the complexity of the mortgage loan settlement process. The process can be improved with simplification of disclosures and better borrower information;

4. Increased shopping by borrowers will lead to greater pricing competition, so that market forces will lower prices and lessen the need for regulatory enforcement;

5. The key final terms of the loan a borrower receives should be disclosed to the borrower in an understandable way at closing; and

6. HUD will continue to vigorously enforce RESPA to protect borrowers and ensure that honest settlement service providers can compete for business on a level playing field.

II. RESPA Overview

Congress enacted the Real Estate Settlement Procedures Act of 1974 (Pub. L. 93–533, 88 Stat. 1724, 12 U.S.C. 2601–2617) after finding that ''significant reforms in the real estate settlement process are needed to ensure that consumers throughout the Nation are provided with greater and more timely information on the nature and costs of the settlement process and are protected from unnecessarily high settlement charges caused by certain abusive practices * * *.'' (12 U.S.C. 2601(a)). RESPA's stated purpose is to ''effect certain changes in the settlement process for residential real estate that will result:

''(1) In more effective advance disclosure to home buyers and sellers of settlement costs;

''(2) In the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services;

''(3) In a reduction in the amounts home buyers are required to place in escrow accounts established to insure the payment of real estate taxes and insurance; and

''(4) In significant reform and modernization of local recordkeeping of land title information.'' (12 U.S.C. 2601(b)).

RESPA's requirements apply to transactions involving ''settlement services'' for ''federally related mortgage loans.'' Under the statute, the term ''settlement services'' includes any service provided in connection with a real estate settlement.[1] The term ''federally related mortgage loan'' is broadly defined to encompass virtually all purchase money and refinance mortgages.[2]

Section 4(a) of RESPA (12 U.S.C. 2603(a)) requires the Secretary to develop and prescribe ''a standard form for the statement of settlement costs which shall be used * * * as the standard real estate settlement form in all transactions in the United States which involve federally related mortgage loans.'' The law further requires that the form ''conspicuously and clearly itemize all charges imposed upon the borrower and all charges imposed upon the seller in connection with the settlement * * *'' (Id).

Section 5 of RESPA (12 U.S.C. 2604) requires the Secretary to prescribe a Special Information Booklet for borrowers. Sections 5(c) and (d) of RESPA require each lender to provide a Good Faith Estimate (GFE), as prescribed by the Secretary, within 3 days of loan application, and that the GFE state ''the amount or range of charges for specific settlement services the borrower is likely to incur in connection with the settlement * * *.''

In 1990, language was added in Section 6 of RESPA (12 U.S.C. 2605) to require certain disclosures to each borrower, both at the time of loan application and during the life of the loan, about the servicing of the loan.

[1] ''Settlement services'' include ''* * * title searches, title examinations, the provision of title certificates, title insurance, services rendered by an attorney, the preparation of documents, property surveys, the rendering of credit reports or appraisals, pest and fungus inspections, services rendered by a real estate agent or broker, the origination of a federally related mortgage loan (including, but not limited to, the taking of loan applications, loan processing, and the underwriting and funding of loans), and the handling of the processing, and closing of settlement.'' 12 U.S.C. 2602(3). The term is further defined at 24 CFR 3500.2.

[2] The term ''federally related mortgage loan'' generally includes a loan that both: (i) Is ''secured by a first or subordinate lien on residential real property (including individual units of condominiums and cooperatives) designed principally for the occupancy of from one to four families''; and (ii) is ''made in whole or in part by any lender the deposits or accounts of which are insured by any agency of the Federal Government, or is made in whole or in part by any lender which is regulated by any agency of the Federal Government''; or ''is made * * * or insured, guaranteed, supplemented, or assisted in any way, by [HUD] or any other officer or agency of the Federal Government or * * * in connection with a housing or urban development program administered by [HUD]'' or other federal officer or agency; or ''is intended to be sold * * * to [Fannie Mae, Ginnie Mae, Freddie Mac], or a financial institution from which it is to be purchased by [Freddie Mac]; or is made in whole or in part by any creditor * * * who makes or invests in residential real estate loans aggregating more than $1,000,000 per year * * *.'' 12 U.S.C. 2602(1).

Section 8(a) of RESPA (12 U.S.C. 2607(a)) prohibits persons from giving and from accepting ''any fee, kickback, or thing of value pursuant to any agreement or understanding, oral or otherwise, that [real estate settlement service business] shall be referred to any person'' (12 U.S.C. 2607(a)). Section 8(b) of RESPA prohibits persons from giving and from accepting ''any portion, split, or percentage of any charge made or received for the rendering of a real estate settlement service * * * other than for services actually performed'' (12 U.S.C. 2607(b)). Section 8(c) provides, in part, that ''[n]othing in [Section 8] shall be construed as prohibiting * * * (2) the payment to any person of a *bona fide* salary or compensation or other payment for goods or facilities actually furnished or for services actually performed, * * * or (5) such other payments or classes of payments or other transfers as are specified in regulations prescribed by the Secretary, after consultation with the Attorney General, the Administrator of Veterans' Affairs, the Federal Home Loan Bank Board,[3] the Federal Deposit Insurance Corporation, the Board of Governors of the Federal Reserve System, and the Secretary of Agriculture'' (12 U.S.C. 2607(c)(2)).

Section 9 of RESPA (12 U.S.C. 2608) forbids any seller of property from requiring, directly or indirectly, buyers to purchase title insurance covering the property from any particular title company. Section 10 of RESPA (12 U.S.C. 2609) limits the amounts that lenders or servicers may require borrowers to deposit in escrow accounts, and requires servicers to provide borrowers with both initial and annual escrow account statements. Section 12 of RESPA (12 U.S.C. 2610) prohibits lenders and loan servicers from imposing any fee or charge on any other person for the preparation and submission of the uniform settlement statement required under Section 4 of RESPA or the escrow account statements required under Section 10(c) of RESPA, or for any statements required by the Truth in Lending Act (TILA).

Section 18 of RESPA (12 U.S.C. 2616) provides that the Act does not annul, alter, affect, or exempt any person from complying with the laws of any State with respect to settlement practices,

[3] The Federal Home Loan Bank Board (FHLBB) was abolished effective October 8, 1989, by the Financial Institutions Reform, Recovery, and Enforcement Act of 1989 (FIRREA) (Pub. L. 101–73, 103 Stat. 183). Its successor agency, the Office of Thrift Supervision, Department of the Treasury, assumed the FHLBB's regulatory functions. 12 U.S.C. 1462a(e).

''except to the extent that those laws are inconsistent with any provision of [RESPA], and then only to the extent of the inconsistency.'' Section 18 further authorizes the Secretary to determine whether such inconsistencies exist, but provides that the Secretary may not determine a State law to be inconsistent with RESPA if the Secretary determines the State law gives greater protection to consumers.

Section 19 of RESPA (12 U.S.C. 2617), among other provisions, authorizes the Secretary to seek to achieve the purposes of RESPA by prescribing regulations, making interpretations, and granting reasonable exemptions for classes of transactions.

III. Overview of HUD's Efforts Since 2002

On July 29, 2002 (67 FR 49134), HUD issued a proposed RESPA reform rule ''Real Estate Settlement Procedures Act (RESPA); Simplifying and Improving the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers'' (2002 Proposed Rule) that would have provided for a revised GFE that would have simplified and standardized estimated settlement cost disclosures to make such estimates more reliable, as well as to prevent unexpected charges at settlement. In addition, the 2002 Proposed Rule would have modified mortgage broker compensation disclosure requirements and would have provided an exemption from Section 8 of RESPA for guaranteed packages of settlement services.

The 2002 Proposed Rule followed several years of consultation with industry, consumer, and government groups on changes to RESPA. The 2002 Proposed Rule also followed two reports to Congress that examined ideas to improve the mortgage loan settlement process: The 1998 joint report by HUD and the Board of Governors of the Federal Reserve (Federal Reserve or the Board) on reform of RESPA and the Truth in Lending Act; and the 2000 HUD-Treasury Report on Predatory Lending. Both of these reports are described in more detail in the 2002 Proposed Rule (see 67 FR at 49143–6).

In response to the 2002 Proposed Rule, HUD received over 40,000 comments, of which 400 contained in-depth discussions of various issues raised by the proposal. Comments were submitted by real estate, mortgage broker, banking, mortgage lending, financial services, and title industry trade groups; consumer advocacy organizations; mortgage companies; settlement service providers; banks; credit unions and related organizations; State agencies; Members of Congress; lawyers; and other concerned persons.

Generally, the extensive comment letters supported the overall goals of the proposal, but disagreed with or expressed reservations concerning specific aspects of the proposal. For example, some lender organizations (including the Mortgage Bankers Association) strongly supported the packaging proposal, while the National Association of Realtors supported the GFE changes. Consumer advocacy organizations (including AARP and the National Consumer Law Center) largely supported the mortgage broker compensation disclosure changes, the other GFE changes; and, subject to some exceptions, the packaging proposal. Several industry organizations supported better disclosure of total mortgage broker compensation. On the other hand, the National Association of Mortgage Brokers opposed HUD's proposed approach to disclosing the yield spread premium as part of the total mortgage broker compensation, and the American Land Title Association opposed HUD's packaging proposal and offered a two-package approach as an alternative.

In response to the considerable and varied comments from the public, as well as from other federal agencies and Congress, the Secretary withdrew the proposed rule in early 2004. At that time, the Secretary committed HUD to gather additional information about settlement service costs and the process of obtaining mortgages, as well as to engage in outreach to Congress, members of potentially affected industries, consumers, and other federal agencies, before proceeding with any proposed changes related to HUD's RESPA regulations.

In June 2004, in preparation for outreach to the industry and consumer groups, HUD began consulting with its federal agency partners, including the Small Business Administration (SBA) Office of Advocacy, on RESPA reform. These meetings continued through 2005. In Spring 2005, HUD also consulted with Members of Congress and congressional staff on RESPA reform.

After these initial consultations, in July and August 2005, HUD held a series of seven consumer and industry roundtables both at HUD Headquarters in Washington, DC, and jointly with the SBA Office of Advocacy in Chicago, Los Angeles, and Fort Worth. As discussed in the public notice announcing the roundtables (70 FR 37646, June 29, 2005), in selecting participants for the roundtables, HUD sought a cross-section of representatives of consumer advocacy organizations, all segments of the settlement services industry, State mortgage industry regulators, and other interested persons who had analyzed the 2002 Proposed Rule or had offered alternative proposals for HUD's consideration. Over 150 companies, organizations, and other persons were invited to attend, and 122 of these attended at least one of the roundtables.

At the roundtables, HUD presented an overview of an approach to RESPA reform that included revision of the GFE, clarification of the yield spread premium disclosure, and the option of providing an exemption from the Section 8 provisions prohibiting referral fees, kickbacks, and unearned fees to encourage packaging of settlement services. After HUD's presentation, participants were encouraged to present their views on RESPA reform issues.

Participants generally agreed that HUD should pursue revision of the GFE. Many participants stated that the GFE should reflect the HUD–1 settlement statement, so that borrowers could better compare the GFE to the HUD–1. Consumer representatives stated that disclosure of the yield spread premium (YSP) is necessary, while mortgage brokers recommended that the YSP disclosure be dropped from the GFE. Mortgage broker participants noted that lenders are not required to disclose any secondary market fees on otherwise identical loans. Mortgage brokers expressed concern that focusing on a requirement for more effective disclosure of YSPs puts mortgage brokers at a severe disadvantage, as compared to lenders, in originating a loan. Lenders maintained that it would be impractical for a lender to disclose on the GFE how much a lender would earn if or when the loan is sold on the secondary market. These concepts also are discussed in more detail in HUD's Real Estate Settlement Procedures Act Statement of Policy 2001–1 (66 FR 53052, at 53256–7, October 18, 2001).

With respect to packaging, small business representatives asserted that a Section 8 exemption for packaging would be harmful to small business providers of settlement services because lenders would dominate packaging and would extract kickbacks from small businesses in exchange for inclusion in a package. Consumer groups opposed packaging with a Section 8 exemption on the grounds that the exemption would provide a safe harbor for loans with high costs and fees and other potentially predatory features. These groups also asserted that there would be no way to determine costs and fees for packaged loans for purposes of determining compliance with the Truth in Lending Act. Lender representatives generally supported packaging under a Section 8 exemption as the most efficient method to ensure cost savings to consumers, but some indicated that packaging could also be delivered with limited Section 8 relief, such as for volume-based discounts and average cost pricing.

IV. This Proposed Rule

A. Generally

Today's proposed rule builds on all of this history and specifically recognizes many of the suggestions made at the roundtables with respect to the GFE and comparability of the HUD–1. The rule proposes a new framework under RESPA that would:

(1) Improve and standardize the GFE form to make it easier to use for shopping among settlement service providers;

(2) Ensure that page one of the GFE provides a clear summary of loan terms and total settlement charges so that borrowers will be able to use the GFE to comparison shop among loan originators for a mortgage loan;

(3) Provide more accurate estimates of costs of settlement services shown on the GFE;

(4) Improve the disclosure of yield spread premiums to help borrowers understand how they can affect their settlement charges;

(5) Facilitate comparison of the GFE and the HUD–1/HUD–1A Settlement Statements (HUD–1 settlement statement or HUD–1);

(6) Ensure that at settlement, borrowers are aware of final loan terms and settlement costs, by reading and providing a copy of a ''closing script'' to borrowers;

(7) Clarify HUD–1 instructions;

(8) Clarify HUD's current regulations concerning discounts; and

(9) Expressly state when RESPA permits certain pricing mechanisms that benefit consumers, including average cost pricing and discounts, including volume-based discounts.

A detailed description of each aspect of the proposed rule that involves these concepts follows in Sections B–E of this preamble.

This proposal also includes certain technical amendments to the current RESPA rules, as set forth below.

B. Legislative Proposals Related to RESPA Reform

In order to further bolster consumer protection, as well as to ensure uniform and consistent enforcement under RESPA, HUD intends to seek legislative changes to RESPA that will complement the regulatory improvements made in this rule. HUD firmly believes that the proposed rule will improve the mortgage loan settlement process through better disclosures to consumers, but greater consumer protection can be achieved by also strengthening certain statutory disclosure requirements and improving the remedies available under RESPA.

In today's proposed rule, HUD seeks to ensure that consumers are provided with meaningful and timely information. While HUD can make certain regulatory improvements to the disclosures that will help consumers shop for mortgage loans, HUD needs additional statutory authority to make further warranted improvements in disclosures that will help consumers understand the final terms of the loans and costs to which they commit at closing. Moreover, as currently framed, RESPA establishes limited and inconsistent enforcement authority, and does not provide HUD with any enforcement authority for key disclosure provisions. The 1998 joint report by HUD and the Federal Reserve on reform of RESPA and the Truth in Lending Act recommended that RESPA be amended to provide for more effective enforcement.[4] In its April 2007 report on the title insurance industry, the Government Accountability Office recommended that Congress consider whether modifications to RESPA are needed to better achieve its purposes, including by providing HUD with increased enforcement authority.[5]

As part of its efforts to improve the protections provided under RESPA, HUD intends to seek statutory modifications that would include the following provisions: (1) Authority for the Secretary to impose civil money penalties for violations of specific RESPA sections, including sections 4 (provision of uniform settlement statement), 5 (GFE and special information (settlement costs) booklet), 6 (servicing), 8 (prohibition against kickbacks, referral fees, and unearned fees), 9 (title insurance), and portions of 10 (escrow accounts), as well as authority for the Secretary and State regulators to seek injunctive and equitable relief for violations of RESPA; (2) requiring delivery of the HUD–1 to the borrower 3 days prior to closing; and (3) a uniform and expanded statute of limitations applicable to governmental and private actions under RESPA.

RESPA does not currently provide HUD with enforcement mechanisms for some of the most important consumer disclosures, including the section 4 requirements related to provision of the HUD–1, and section 5 requirements related to provision of the GFE and the special information (settlement costs) booklet. HUD believes that a lack of enforcement authority and of clear remedies for violations of critical sections of RESPA negatively impacts consumers and diminishes the effectiveness of the statute. Accordingly, HUD intends to seek authority to impose civil money penalties to enforce violations of RESPA. In addition to civil money penalty authority, HUD intends to seek authority for additional injunctive and equitable remedies for violations of RESPA.

Improving the ability of consumers to shop for the best mortgage loan and control settlement costs—using the new GFE form and comparing it to the HUD–1 at closing—is a key component of today's proposed rule. Additional statutory authority would enable HUD to improve its efforts at providing borrowers with necessary and timely information about their mortgage loans and other settlement services. Section 4 of RESPA currently provides that a borrower may request to inspect the HUD–1 the day before settlement, but many borrowers are unaware of this right, and the time currently provided to inspect the HUD–1 allows little margin for identifying and challenging problematic charges before settlement.

HUD also intends to seek reform of the statute of limitations provisions of RESPA. Currently, there are different limitation periods depending on which section of the statute is alleged to have been violated, and who is pursuing a remedy of the violation. HUD believes that enforcement efforts would be enhanced, and the requirements of the statute simplified, by standardizing the statute of limitations.

C. Federal Reserve Board Proposed Rule Amending Regulation Z

On January 9, 2008, the Federal Reserve Board (Board) issued a proposed rule that would amend its Regulation Z which implements the Truth in Lending Act, 16 U.S.C. 1601, *et seq.* (73 FR 1672, January 9, 2008). The proposed rule is intended to accomplish three goals: (1) To protect consumers in the mortgage market from unfair, abusive, or deceptive lending and servicing practices while preserving responsible lending and sustainable homeownership; (2) to ensure that mortgage loan advertisements provide accurate and balanced information and

[4] See Section III of this preamble.

[5] *Title Insurance: Actions Needed to Improve Oversight of the Title Industry and Better Protect Consumers,* Government Accountability Office, April 2007, GAO–07–401.

do not include misleading or deceptive representations; and (3) to require earlier mortgage disclosures for non-purchase money mortgage transactions which would include mortgage refinancings, closed-end home equity loans, and reverse mortgages (73 FR 1672).

In its proposal, the Board would establish new protections for higher-priced mortgages, a newly defined category of loans, and for all mortgage loans. The proposed rule contains four key protections for higher-priced mortgage loans to prohibit creditors from: (1) Engaging in a pattern or practice of extending credit based on the collateral without regard to the consumer's ability to repay; (2) making a loan without verifying the income and assets relied upon to make the loan; (3) imposing prepayment penalties in certain circumstances; and (4) making loans without establishing escrows for taxes and insurance (73 FR 1673).

The Board also proposes, for all mortgage transactions, to prohibit creditors from paying mortgage brokers more than the consumer agreed the broker would receive. Specifically, the proposed rule would prohibit a creditor from making a payment, ''directly or indirectly, to a mortgage broker unless the broker enters into an agreement with a consumer'' (73 FR 1725). Further, a creditor payment to a mortgage broker could not exceed the total amount of compensation stated in the written agreement, reduced by any amounts paid directly by the consumer or by any other source (Id).

In proposing the mortgage broker agreement, the Board recognizes HUD's current policy statements and regulatory requirements regarding disclosure of mortgage broker compensation and noted that HUD had announced its intention to propose improved disclosures under RESPA (73 FR 1700). The Board stated that it intends that its proposal ''* * * would complement any proposal by HUD and operate in combination with that proposal to meet the agencies' shared objectives of fair and transparent markets for mortgage loans and for mortgage brokerage services.''

HUD believes its proposals regarding the GFE and mortgage broker compensation are consistent with those of the Board. As HUD moves forward to finalize this rule, it will continue to work with the Board to make the respective rules consistent, comprehensive, and complementary.

D. Planned Implementation of Final Rule

Given the significant changes that would be made in its RESPA regulations by this proposed rule, the Department intends to include a transition period in the final rule. During the 12-month transition period, settlement service providers and other persons may comply with either the current requirements or the revised requirements of the amended provisions. HUD is seeking comments on whether such a transition period is appropriate.

E. The GFE and GFE Requirements

Problems Identified with the Existing GFE. Under RESPA, loan originators must provide a GFE of the borrower's settlement costs (along with HUD's Special Information Booklet in home purchase transactions) at or within 3 days of a mortgage loan application. RESPA authorizes HUD to prescribe regulations concerning the GFE, and HUD's regulations at 24 CFR 3500.7, along with the suggested format set forth in Appendix C to the regulations, constitute the current GFE guidance. At the closing, a borrower must receive the Uniform Settlement Statement (HUD–1 or HUD–1A), which itemizes final settlement charges to borrowers. The regulations at 24 CFR 3500.8–3500.10 and the instructions in Appendix A to the regulations specify HUD's requirements for the HUD–1/1A.

HUD believes that the GFE could better facilitate borrowers shopping for the best loan. Further, the GFE could better achieve the statute's purposes of preventing unnecessarily high settlement costs by requiring a more accurate and consistent presentation of costs. The regulations do not require that the GFE be given to the borrower until after he or she submits a full application to an originator. This can result in a borrower paying significant fees before receiving a GFE, inhibiting the possibility of shopping beyond the provider with whom the applicant first applies. HUD's RESPA regulations require that the GFE include a list of charges but they do not prescribe a standard form. Consequently, it is virtually impossible to shop and compare the charges of various originators and settlement service providers using the GFE, because different originators may list different types or categories of charges, or may identify specific charges by different names, or both. The current regulations also do not require that the GFE contain information on the terms of loans, such as the loan's interest rate, for purposes of comparison. Further, while the HUD Special Information Booklet supplements the GFE, the GFE does not provide certain important explanatory information to the borrower including, for example, how the borrower can use the document to shop and compare loans. The GFE also does not make clear the relationship between the closing costs and the interest rate on a loan.

HUD's current regulations require loan originators to list on the GFE the ''amount of or range of'' each charge that the borrower is likely to incur in connection with the settlement.[6] The suggested GFE format, found in Appendix C to the regulations, lists 20 common settlement services. The suggested format also provides a space for listing any other applicable services and charges. These requirements have led, in many instances, to a proliferation of charges for separate ''services'' without any actual increase in the work performed by individual settlement service providers.

The RESPA regulations do not require that the GFE clearly identify the total charges of major providers of settlement services, including lenders and brokers (loan originators), title agents and insurers (title charges), and other third party settlement service providers. Without the simplification provided by presenting totals for major items, it is difficult for borrowers to know how much they are paying for major items, including origination and title related charges, or how they can compare loans and select among service providers to get the best value.

The estimated costs on GFEs are frequently unreliable or incomplete, or both, and final charges at settlement often include significant increases in items that were estimated on the GFE, as well as additional surprise ''junk fees,'' which can add substantially to the consumer's ultimate closing costs.

New GFE Requirements. In light of these considerations, HUD believes that in order for the GFE to better serve its intended purpose, which is to apprise borrowers of the charges they are likely to incur at settlement, a number of specific changes to the GFE requirements are required to make it firmer and more useable. Accordingly, today's proposed rule would establish a new required GFE form to be provided to borrowers by loan originators in all RESPA covered transactions.[7] HUD

[6] 24 CFR 3500.7(a).

[7] HUD's RESPA rules currently provide that in the case of a federally related mortgage loan involving an open-end line of credit (home equity plan) covered under the Truth in Lending Act and Regulation Z, a lender or broker that provides the borrower with the disclosures required by 12 CFR

believes that the content of the material in the proposed form gives the consumer the information needed to shop for loan products and to assist them during the settlement process. The Department seeks public comment on the proposed GFE, as well as the proposed HUD–1/1A Settlement Statement forms. The following sections address the proposed changes, and, where appropriate, include a summary of comments received on the issue in response to the 2002 Proposed Rule, as well as comments voiced during the 2005 RESPA Reform Roundtables.

1. Changes to Facilitate Shopping

The Proposed Rule. Today's rule proposes to establish a new definition for a ''GFE application'' and a separate new definition for ''mortgage application.'' The GFE application would be comprised of those items of information that the borrower would submit to receive a GFE. Such an application would include only such information as the originator considered necessary to arrive at a preliminary credit decision and provide the borrower a GFE. Specifically, a GFE application would include six items of information (name, Social Security number, property address, gross monthly income, borrower's information on the house price or best estimate of the value of the property, and the amount of the mortgage loan sought) in order to enable a loan originator to make a preliminary credit decision concerning the borrower. The proposed rule will also require that the GFE application be in writing or in computer-generated form. Oral applications can be accepted at the option of the lender. In such cases, the lender must reduce the oral application to a written or electronic record.

The proposed rule also provides that when a borrower chooses to proceed with a particular loan originator, the loan originator may require that the borrower provide a ''mortgage application'' to begin final underwriting. The mortgage application will ordinarily expand on the information provided in the GFE application, including bank and security accounts and employment information as well as asset and liability information and all the other information that the originator requires to underwrite the loan.

To facilitate shopping and lower the cost burden of shopping on consumers and industry alike, the proposed rule would not require that all underwriting information be supplied at the GFE application stage. Nevertheless, borrowers must be protected against ''bait and switch.'' Accordingly, the proposed rule provides that during final underwriting, the originator may verify the information in and developed from the GFE application, including employment and income information, ascertain the value of the property to secure the loan, update the credit analysis, and analyze any relevant information collected in the entire application process, including, but not limited to, information on the borrower's assets and liabilities. However, borrowers may not be rejected unless the originator determines that there is a change in the borrower's eligibility based on final underwriting, as compared to information provided in the GFE application and credit information developed for such application prior to the time the borrower chooses the particular originator.[8] The originator must document the basis for any such determination and keep these records for no less than 3 years after settlement, in accordance with proposed subsection 24 CFR 3500.7(f)(1)(iii).

Where a borrower is rejected for a loan for which a GFE has been issued, and another loan product is available to the borrower, the loan originator must provide the borrower with a revised GFE. Where a borrower is rejected, the borrower must be notified within one business day and the applicable notice requirements satisfied.

Loan originators will provide GFEs based on the GFE applications that are memorialized in writing or electronic form. A separate GFE must be provided for each loan where a transaction will involve more than one mortgage loan. For loans covered by RESPA, Truth in Lending Act (TILA) disclosures would also be provided within 3 days of a written GFE application, unless the creditor, i.e., loan originator, determines that the application cannot be approved on the terms requested. (See comments 19(a)(1)–3 and 4 of the Federal Reserve Board's Official Staff Commentary on the Truth in Lending Act (TILA).) Based on consultations with representatives of the Federal Reserve, when a GFE application is submitted, an initial TILA disclosure should also be provided so long as the application is in writing, or, in the case of an oral application, committed to written or electronic form.

By obtaining multiple GFEs, borrowers will be in a position to decide which loan provider and which mortgage product they wish to select. When the borrower makes those decisions, the borrower will notify the originator, who may then require a more comprehensive ''mortgage application,'' and possibly a fee or fees, to initiate the loan origination. As indicated, this application would consist of the more detailed information required by the originator, submitted in order to obtain a final underwriting decision, leading to origination of a mortgage loan.[9]

Discussion. Under RESPA, a GFE must be provided to a borrower at or within 3 days of application. HUD's current regulations define an application as the ''submission of a borrower's financial information in anticipation of a credit decision, whether written or computer generated, relating to a federally related mortgage loan'' identifying a specific property.[10] The 2002 Proposed Rule sought to make GFEs more readily available to consumers and, therefore, more useful as a shopping tool by clarifying the minimum information needed to obtain a GFE and by broadening the rules to allow oral applications, consistent with earlier informal interpretations by HUD, so long as such requests contained sufficient information for the originator to provide a GFE. Accordingly, the 2002 Proposed Rule also revised the definition of ''application'' in the regulations to make it clear that an application would be deemed to exist, and that the GFE should be provided once the consumer provided sufficient information to enable a loan originator to make an initial determination regarding the borrower's creditworthiness (typically, a Social Security number, a property address, basic income information, the borrower's information on the house price or best estimate of the value of the property, and the mortgage loan amount needed), whether orally, in writing or computer-generated. The GFE would be given to the borrower, conditioned on final loan approval following full underwriting and appraisal of the property securing the mortgage.

HUD acknowledged in the 2002 Proposed Rule that the proposed changes in the definition of ''application'' and the requirement that a GFE be provided to prospective borrowers early in the shopping process

226.5b of Regulation Z at the time the borrower applies for such loan shall be deemed to comply with GFE requirements set forth at 24 CFR 3500.7. Nothing in this proposed rule is intended to change this provision.

[8] Unforeseeable circumstances resulting in a change in the borrower's eligibility may also be a basis for rejecting the borrower. Unforeseeable circumstances are also discussed in Section 8(b) below.

[9] HUD anticipates that in most cases a mortgage application will be the Uniform Residential Loan Application, Freddie Mac Form 65, or Fannie Mae Form 1003.

[10] 24 CFR 3500.2.

might have implications for the content and delivery of required disclosures under TILA requirements. As a result, HUD invited comments on how the proposed GFE changes might impact other disclosure requirements, and also invited comments on how the proposed GFE changes could be harmonized with the other disclosure requirements.

As indicated above, under today's proposal, the definition of ''GFE application'' provides the trigger for initial RESPA disclosures. After a consumer decides to proceed with a particular loan originator's GFE, the loan originator will generally require a separate ''mortgage application'' as defined under this proposed rule, before making a credit decision. Consumer representatives recommended that HUD consult with the Federal Reserve Board to coordinate the timing of RESPA and TILA disclosures. Industry commenters on the 2002 Proposed Rule were generally concerned that HUD's proposal to require disclosures earlier in consumers' process of shopping for a mortgage would trigger requirements under the Home Mortgage Disclosure Act (HMDA) and the Equal Credit Opportunity Act (ECOA).

By refining the definition of ''application'' under RESPA, and dividing the application process as described, HUD believes that today's proposal will facilitate the availability of shopping information and avoid unnecessary regulatory burden on the industry and an unwarranted increase in notices of loan denials to borrowers. Whether a GFE application under a particular set of facts triggers HMDA or ECOA requirements must be determined under Regulation B and Regulation C, as interpreted in the Federal Reserve Board's official staff commentary. It should be noted that by proposing such a change to the current definition of ''application,'' HUD does not intend to prevent a loan originator from prequalifying a borrower for a mortgage loan.

2. Addressing Up-Front Fees That Impede Shopping

The Proposed Rule. The proposal would allow a loan originator, at its option, to collect a fee limited to the cost of providing the GFE, including the cost of an initial credit report, as a condition for providing a GFE to the prospective borrower.

Discussion. HUD would prefer that originators not impose any charges for a GFE, since providing a GFE before the payment of any fee will further facilitate shopping. HUD believes it would be reasonable for loan originators to treat shoppers for mortgages in much the same way other retailers treat shoppers, where the price of the product includes marketing expenses and purchasers pay the cost incurred to serve shoppers who do not purchase the goods or services. Such an approach would better serve the purposes of the statute. However, HUD recognizes that there may be incidental or nominal costs to provide GFEs to prospective borrowers. Therefore, in order to facilitate shopping using GFEs, the proposed rule would allow a loan originator, at its option, to collect a fee limited to the cost of providing the GFE, including the cost of an initial credit report, as a condition for providing a GFE to a prospective borrower. HUD is interested in receiving comments on this approach.

3. Introductory Language

The Proposed Rule. The proposed GFE explains to the borrower: (1) The purpose of the GFE, i.e., that it is an ''* * * estimate of your settlement costs and loan terms if you are approved for this loan'' and (2) informs the borrower that he or she is the ''* * * only one who can shop for the best loan for you. You should compare this GFE with other loan offers. By comparing loan offers, you can shop for the best loan.''

Discussion. The GFE proposed today informs the borrower that he or she is the only one who can shop for the best loan. HUD believes that this formulation should be useful to consumers dealing with all types of loan originators.

The 2002 Proposed Rule had included language in this section of the previously proposed GFE that was intended to describe the role of the loan originator and to encourage borrowers to shop for themselves. Comments both from consumer groups and industry generally favored removing language on the GFE that discussed the role of the loan originator, on the grounds that the language was misleading, confusing, and might conflict with state law. AARP, however, supported retaining the portion of the proposed language that encourages the borrower to shop among loan originators.

In light of the comments received on the 2002 proposal, today's proposed GFE does not include any language on the role of the loan originator. Instead, the language on the proposed GFE informs the consumer that he or she is the only one who can shop for the best loan.

4. Terms on the GFE (Summary of Loan Details)

The Proposed Rule. The proposed GFE includes a summary of the key terms of the loan. The form discloses the initial loan amount; the loan term; the initial interest rate on the loan; the initial monthly payment owed for principal, interest, and any mortgage insurance; and the rate lock period. The form also discloses whether the interest rate can rise, whether the loan balance can rise; whether the monthly amount owed for principal, interest and any mortgage insurance can rise; whether the loan has a prepayment penalty or a balloon payment and whether the loan includes a monthly escrow payment for property taxes and possibly other obligations. HUD is requiring the terms ''prepayment penalty'' and ''balloon payment'' to be interpreted consistent with TILA (15 U.S.C. 1601 *et seq.*). The Annual Percentage Rate (APR) is not included on the proposed GFE.

Discussion. One of HUD's objectives in proposing revisions to the current RESPA regulations is to ensure that consumers are able to use page one of the GFE to comparison shop among loan originators for a mortgage loan. Accordingly, page one of the proposed GFE contains a summary of the loan terms and details, as well as a summary of the total estimated settlement charges for the loan. The new summary format of page one of the proposed GFE with its list of important loan terms will increase consumer awareness and allow borrowers the opportunity to shop among loan originators and easily compare various loan offers.

The proposed GFE is designed to provide clear information on both fixed and adjustable rate mortgages. The disclosure of terms on the latter is complicated due to their variable structure and to future changes in interest rates. Adjustable rate mortgages have recently experienced high default rates. HUD seeks comment on possible additional ways to increase consumer understanding of adjustable rate mortgages.

The 2002 proposed GFE advised the borrower of the terms of the mortgage and included the interest rate and the APR. It also advised the borrower whether or not the loan had a prepayment penalty or balloon payment, and whether the loan had an adjustable rate and, if so, its terms. Comments on the 2002 GFE primarily concerned whether it should include information also appearing on the TILA disclosure. Consumers generally supported the inclusion of TILA disclosure information on the GFE. Lenders generally recommended that information appearing on TILA disclosures should be removed from the GFE because borrowers will continue to receive separate TILA disclosure forms, and inclusion on the GFE is unnecessary and would potentially lead to borrower confusion. Some participants at the RESPA Reform Roundtables suggested that more information on new loan products such as interest-only loans should be included on the GFE.

While mindful of the need to present consumers with key loan information on the GFE, HUD has determined not to include the APR on today's proposed GFE. The APR is central to the TILA disclosure that will be provided in purchase transactions at the same time as the GFE and ordinarily at the same time in other transactions. However, the terms ''prepayment penalty'' and ''balloon payment'' have been retained on the form to facilitate consumer shopping, even though these terms are also included on the TILA disclosure.

With respect to today's proposed GFE, HUD notes that there are differences between how the GFE discloses the monthly payment and how the TILA form will disclose the monthly payment. Specifically, the proposed GFE requires disclosure of principal, interest, and any mortgage insurance, while the TILA disclosure may include amounts for taxes. HUD will revise its Special Information Booklet to explain this difference, to avoid consumer confusion.

The interest rate listed on the GFE will reflect the loan offered at the time the GFE is given. Until locked in, the interest rate will float. For loans originated by mortgage brokers, the amount of any ''charge or credit to the borrower for the specific interest rate chosen'' will float with the wholesale market.[11] This is because mortgage brokers must report the precise difference between the price of the loan and its par value in the ''charge or credit for the specific interest rate chosen.'' As a result, borrowers who use brokers as defined in this proposed rule and choose to float will float according to wholesale lenders' changes.

Current federal regulations allow originators to provide GFE and TILA information together.[12] However, the proposed GFE is designed as a distinct, required form to promote shopping by consumers. HUD believes it is best complemented by providing a separate TILA disclosure along with the GFE.

5. Period During Which the GFE Terms Are Available to the Borrower

The Proposed Rule. The interest rate stated on the GFE would be available until a date set by the loan originator for the loan. After that date, the interest rate, some of the loan originator charges, the per diem interest, and the monthly payment estimate for the loan could change until the interest rate is locked. The estimate of the charges for all other settlement services would be available until 10 business days from when the GFE is provided, but it may remain available longer, if the loan originator extends the period of availability.

Discussion. In order to promote competition while avoiding committing originators to open-ended offers, the 2002 Proposed Rule would have required that the GFE be held open for a minimum of 30 days. Commenters on the 2002 Proposed Rule were specifically asked whether 30 days was an appropriate period, and considerable comment was elicited on this subject. A major consumer group supported the 30-day period, while the majority of lenders commenting on the 2002 proposal recommended a 10-day shopping period or less.

Today's proposed rule reflects HUD's determination that the appropriate period for which GFE terms are generally to be available is 10 business days, excluding the interest rate of the loan set forth in the GFE, some of the loan origination charges related to the interest rate, the per diem interest, and the monthly payment estimate. The interest rate stated on the GFE would be available until a date set by the loan originator for the loan. After that date, the interest rate, some of the loan originator charges, the per diem interest, and the monthly payment estimate for the loan could change until the interest rate is locked.

A central purpose of RESPA regulatory reform is to facilitate shopping in order to lower settlement costs, and there is legitimate concern that requiring GFEs to be open for too long a shopping period could unintentionally operate to increase borrower costs. By requiring that the GFE terms be generally available for 10 business days, GFEs will be effectively open for 2 weeks, thereby providing borrowers with sufficient time to shop among various offers and providers. Borrowers may request, and originators at their option may lengthen the shopping period for a loan or loans beyond 10 business days. In such cases, the originator should note and initial the increased duration the GFE is open on the borrower's GFE.

6. Consolidating Major Categories on the GFE

The Proposed Rule. The proposed GFE would group and consolidate all fees and charges into major settlement cost categories, with a single total amount estimated for each category.

Discussion. Under current RESPA rules, the GFE simply lists estimated charges or ranges of charges for settlement services. There is no requirement for grouping or subtotaling charges to the same recipients. The costs listed on the GFE include loan originator charges such as loan origination and underwriting charges; charges by third parties for lender-required services, such as appraisal, title, and title insurance fees; state and local charges imposed at settlement such as recording fees or city/county stamps; and amounts the borrower is required to put into an escrow account, or reserves, for items such as property taxes or hazard insurance. At settlement, borrowers receive a second RESPA disclosure—the Uniform Settlement Statement (the HUD–1/1A) that enumerates the final costs associated with both the loan and, if applicable, the purchase transaction.

The proposed GFE would group and consolidate all fees and charges into major settlement cost categories, with a single total amount estimated for each category. This approach would reduce any incentive for loan originators and others to establish a myriad of ''junk fees'' and provide them in a long list in order to increase their profits.

In the 2002 Proposed Rule, HUD had proposed a GFE that grouped and consolidated charges into major cost categories, with a single total amount for each category. In commenting on the 2002 proposal, consumer groups were split on the best approach to addressing fee proliferation on the GFE. AARP strongly supported consolidation of major cost categories, and recommended that HUD's proposed categories be further consolidated into three categories for enhanced consumer comprehension. The National Consumer Law Center (NCLC) filed comments on its own behalf, and on behalf of the Consumer Federation of America, National Association of Consumer Advocates, Consumers Union, and U.S. Public Interest Research Group. These commenters noted that while subtotaling is helpful to consumers, itemization on the HUD–1 is necessary to ensure that compliance with TILA and the Home Ownership and Equity Protection Act (HOEPA) can be determined. The National Community Reinvestment Coalition and the National Center on Poverty Law indicated their belief that the

[11] The ''charge or credit for the interest rate chosen'' concerns the discount points and the yield spread premium that are further discussed in Section C of this preamble.

[12] 24 CFR 3500.7(d).

tolerance[13] levels will address the issue of proliferation of fees, and commented that the GFE must be as similar as possible to the HUD–1 for comparison purposes. Lenders who commented on this proposed change to the GFE in 2002 expressed concern that lumping costs together in large categories will confuse consumers when they compare data on the GFE with data on the HUD–1/1A.

Having considered the results of consumer testing of the forms as detailed below in Section F and comments received on the 2002 Proposed Rule, HUD has determined to propose a standardized GFE, containing major cost categories, to facilitate better borrower understanding of settlement services and their costs, and empower borrowers to shop, compare, and negotiate major cost items where possible. HUD is not proposing to further consolidate the categories, because it believes that each of the proposed categories provides useful information to borrowers. Although today's proposed GFE does not itemize the services required in each category, it does explain to the borrower the exact nature of each category of services. For example, origination services are characterized as the services and charges to obtain and process the loan for the borrower. HUD also regards the information on required services that can and cannot be shopped for as useful information that borrowers should have in choosing an originator and later to facilitate shopping for services to lower costs.

HUD's current RESPA regulations require that the GFE include a list of any lender-required providers, including the name, address and telephone number of the provider and the nature of the lender's relationship with the provider. Under today's proposed rule, if the lender requires the use of a particular provider other than its own employees, and requires the borrower to pay any portion of such service, the lender must identify on the GFE the service, and the estimated cost or range of charges for the service. HUD has determined to eliminate the requirement to identify the name of the required service provider, because it believes that consumers will use the GFE to shop among loan originators based on cost rather than on the identity of individual settlement service providers.

Where a lender permits a borrower to shop for a required settlement service, under today's proposed rule the lender must provide the borrower with a written list of identified providers at the time the GFE is provided. Such a list may be included on the GFE form or on a separate sheet of paper.

The GFE set forth in the 2002 Proposed Rule would also have referenced the corresponding series on the HUD–1, to facilitate comparison between the GFE and HUD–1. While these references have been removed in the GFE proposed today in the interest of simplifying the form, HUD is also proposing changes to the HUD–1/1A to facilitate comparison of the GFE to the HUD–1/1A. Section II.D. of this preamble discusses today's proposed changes to the HUD–1/1A.

Pursuant to 24 CFR 3500.15, originators seeking to satisfy the requirements for the affiliated business exemption must provide the requisite affiliated business arrangement disclosure at the time of any referral to an affiliated settlement service provider. The GFE proposed by today's Proposed Rule does not attempt to include this information. However, under HUD's existing RESPA regulations, the affiliated business disclosure must be given on a separate form consistent with Appendix D of HUD's existing regulations. Where such a referral occurs at the time a GFE is given, the affiliated business disclosure must be given along with the GFE.

7. Option to Pay Settlement Costs

The Proposed Rule. The GFE Form shall advise the borrower how the interest rate of the loan affects the borrower's settlement costs, and shall include actual available options in this regard on the form.

Discussion. In addressing the problem of lender payments to mortgage brokers in the 1999 and 2001 Policy Statements,[14] HUD made it clear that consumers should be advised as early as possible when shopping for a loan of how their interest rate affects their settlement costs and that their options in this regard should be presented on the GFE form. In order to decide which rate/cost combination is best, HUD regards it as essential that borrowers be presented actual offers of the loan originator on the chart on page 3 of today's proposed GFE. The GFE would inform borrowers that: (1) They can choose the loan presented in the GFE; (2) they can choose an otherwise identical loan with a lower interest rate and monthly payments that will raise settlement costs by a specific amount; or (3) they can choose an otherwise identical loan with a higher interest rate and monthly payments that will lower settlement costs by a specific amount. If a higher or lower interest rate is not in fact available from the originator, the originator must provide those options that are available and indicate ''not available'' on the form for those options that are not available. While some commenters on the 2002 Proposed Rule recommended that HUD require loan originators to feature specific types of loans on the loan option chart on the GFE, HUD does not believe that it should impose requirements on loan originators on what types of loans are offered to borrowers. Therefore, HUD does not propose such requirements in today's proposed rule. HUD's consumer testing has demonstrated that consumers responded very positively to the trade-off chart on the GFE that presents information on different interest rates and up-front fees. In fact, this was the feature that consumers liked best about the form.

The provision of this information on page 3 of the form will help borrowers understand their options for paying settlement costs. If the borrower chooses one of the two alternative options presented on the form, the borrower must receive a new GFE.

8. Establishing Meaningful Standards for GFEs

a. Tolerances.

The Proposed Rule. The proposal would prohibit loan originators from exceeding at settlement the amount listed as ''our service charge'' on the GFE, absent unforeseeable circumstances. The charge or the credit to the borrower for the interest rate chosen, if the interest rate is locked, absent unforeseeable circumstances, also cannot be exceeded at settlement. The proposal would also prohibit Item A on the GFE, ''Your Adjusted Origination Charges'' from increasing at settlement once the interest rate is locked. In addition, the proposal would prohibit government recording and transfer charges from increasing at settlement, absent unforeseeable circumstances. The proposal would prohibit the sum of all the other services subject to a tolerance (originator required services where the originator selects the third party provider, originator required services where the borrower selects from a list of third party providers identified by the originator, and optional owner's title insurance, if the borrower uses a provider identified by the originator) from increasing at settlement by more than 10 percent absent unforeseeable

[13] ''Tolerance'' refers to the maximum amount by which the charge for a category of settlement costs may exceed the amount of the estimate for such category on a GFE, and is expressed as a percentage of an estimate. See Section (h) below.

[14] 64 FR 10080 (March 1, 1999), 66 FR 53052 (October 18, 2001).

circumstances. Thus, a specific charge may increase by more than 10 percent at settlement, so long as the sum of all the services subject to the 10 percent tolerance does not increase by more than 10 percent.

Discussion. Current RESPA regulations at 24 CFR 3500.7(a) require a lender to provide a ''good faith estimate'' of the ''amount of or range of charges for the specific settlement services the borrower is likely to incur in connection with the settlement.'' While the rules require that the estimate be made ''in good faith'' and ''bear a reasonable relationship'' to the charges the borrower is likely to incur at settlement, HUD is proposing to clarify what a ''Good Faith Estimate'' demands, both with regard to the loan originator's own charges, as well as to lender-selected, third party charges and other settlement costs.

Estimates appearing on the GFEs can be significantly lower than the amount ultimately charged at settlement and do not provide meaningful guidance on the costs borrowers will incur at settlement. While unforeseeable circumstances can drive up costs in particular circumstances, in most cases loan originators have the ability to estimate final settlement costs with great accuracy. The loan originator's own charges, which are entirely within the originator's control, can be stated with certainty, absent unforeseeable circumstances. Government recording and transfer charges are well known to loan originators or can be calculated based on the purchase price or value of the property. Moreover, many third party costs such as credit report fees, pest inspection fees, tax services, and flood reviews are readily ascertainable. Other third party costs such as title services and title insurance and up-front mortgage insurance premiums, typically only vary depending on the value of the property or the loan amount. HUD also is aware that recent advances in technology and telecommunications in loan processing make routine provision of accurate estimates of third party costs easier and cheaper.

Some borrowers have indicated that the GFE has often failed to represent an accurate estimate of final settlement costs, for a number of reasons. In too many cases, fees that were not included on the GFE materialize at settlement. These unexpected fees often result in extra compensation for the originator and/or the third party settlement service providers and in higher charges to the borrower. The absence of more precise regulatory standards for providing a good faith estimate of final settlement costs has not helped ensure greater accuracy and reliability.

In light of these considerations, HUD believes that in order for the GFE to serve its intended purpose, which is to apprise prospective borrowers of the charges they are likely to incur at settlement, new standards must be established under existing law to better define good faith'' and the standards applicable to the GFE.[15] Accordingly, the proposed rule states that loan originators may not increase their own charges (the service charge) from that stated on the GFE, absent ''unforeseeable circumstances.'' Government recording and transfer charges would also not be able to increase at settlement, absent ''unforeseeable circumstances.'' While the interest rate is locked, the charge or the credit to the borrower for the interest rate chosen also cannot be exceeded at settlement, absent ''unforeseeable circumstances.'' While fees for the service charge have a ''zero tolerance'' under the proposed rule, absent unforeseeable circumstances, the sum of all the other services subject to a tolerance—required services the loan originator selects, title and closing services, lender's title insurance and optional owner's title insurance if chosen or identified by the originator, and required services that borrowers can shop for when the borrower elects to use the provider identified by the originator—would be subject to a single overall 10 percent tolerance. Thus, a specific charge may increase by more than 10 percent, so long as the total does not increase by more than 10 percent.

The subject of tolerances received considerable attention from commenters in the 2002 proposed RESPA rulemaking, as well as during the RESPA Reform Roundtables. Generally, lending industry groups commenting on the 2002 Proposed Rule opposed tolerances on the grounds that settlement costs are extremely variable and subject to change after appraisal and underwriting. Many other comments from lenders on the 2002 Proposed Rule noted that costs often change after property appraisal and as a result of borrower product changes or changes in the loan amount or closing date. Consumer groups, on the other hand, supported tolerances as a means to prevent ''bait and switch'' tactics by loan originators. Regulators, including the Conference of State Bank Supervisors and the American Association of Residential Mortgage Regulators, were generally supportive of tolerances. During the RESPA reform roundtables, many participants who expressed comments on the need for tolerances agreed that it is possible to get solid estimates of costs at the GFE stage, while others expressed concern that a 10 percent tolerance level is too strict.

In its written comments in response to the 2002 Proposed Rule, the American Land Title Association (ALTA) questioned HUD's authority to adopt tolerances in light of the legislative history of the good faith estimate requirement in Section 5(c) of RESPA. ALTA noted that as part of the original RESPA statute, Congress enacted a separate section that required lenders, at the time of loan commitment, but not later than 12 days prior to settlement, to provide the prospective buyer and seller with an ''itemized disclosure in writing of each charge arising in connection with the settlement.'' Section 6 of the original statute imposed a duty on the lender to obtain from persons who were to provide services in connection with the settlement ''the amount of each charge they intend to make.'' If the exact charge was not available, a good faith estimate could be provided. Section 6(b) provided for lender liability to the buyer or seller for failure to provide the requisite disclosures in the amount of actual damages or $500, whichever was greater, and, if the action was successful, attorney's fees and court costs.

ALTA noted that due to concerns raised by lenders about Section 6, that provision of RESPA was repealed within one year of enactment. Congress substituted for Section 6 the language of Section 5(c) requiring lenders to provide a good faith estimate of settlement costs, along with a Special Information Booklet, within 3 days of loan application. ALTA also noted that Congress did not impose any sanctions for violations of the Section 5(c) obligation. In light of this legislative history, ALTA contends that HUD does not have statutory authority to adopt tolerances as proposed.

While mindful of the legislative history of RESPA with respect to the enactment and later repeal of the section requiring lenders to provide disclosures of the amount of each charge arising in

[15] Differing editions of Black's Law Dictionary have defined ''good faith'' as a ''state of mind consisting in * * * honesty in belief or purpose * * * and faithfulness to one's duty or obligation,'' and ''freedom from knowledge of circumstances which ought to put the holder upon inquiry,'' as well as ''absence of all information, notice, or benefit or belief of facts which render a transaction unconscientious.'' Inherent in these definitions is the concept that where a party makes an estimate in good faith, the party will take into account all available relevant information, and will exercise reasonable care in evaluating such information before providing such an estimate.

connection with the settlement, HUD believes that the tolerance approach it is proposing today is distinguishable from the requirement to provide an itemized disclosure of each charge. Unlike the requirement in the original Section 6 of RESPA that required lenders to provide exact figures for individual settlement charges, today's proposed approach permits considerable flexibility. The proposal would permit all charges to decrease between the time the GFE is provided and the date of settlement; all charges may increase in the event of unforeseeable circumstances; and some third party charges such as homeowners' insurance are not subject to any tolerance. Moreover, individual charges for certain third party services that originators require and either select or identify may increase by more than 10 percent at settlement, as long as the sum of such charges increases by no more than 10 percent at settlement.

In considering the appropriate tolerance for third party settlement services on the GFE, HUD considered the available data on the variation in the cost of title services within individual market areas. Title services is the largest component of third party settlement service costs, accounting for slightly over two-thirds of the total among the sample of Federal Housing Administration (FHA) insured-loans discussed in the Economic Analysis. A study by Consumers Union on the dispersion of title costs within each of five large California metropolitan areas provides the best available data. Consumers Union found that, for four of the five metropolitan areas—Los Angeles, San Francisco, San Diego, and Sacramento—the highest reported prices for title services were between 9.95 percent and 13.84 percent above the average price in the local market. The exception is Fresno, where the highest price is 27.90 percent above the average. These data indicate that a title insurance company should be able to remain within about 10 percent of its originally quoted price, in the event that a particular loan turns out to involve more extensive title work than originally anticipated. HUD therefore has concluded that a 10 percent tolerance is reasonable. To provide a further margin for unexpected cost increases, HUD extended the 10 percent tolerance per service in the 2002 Proposed Rule to a 10 percent tolerance for the combined total cost of all third party settlement services selected by the lender. Other services are a much smaller share of the total cost of third party settlement services, and therefore increases in their cost are likely to have a much smaller impact on the combined total cost of all third party settlement services covered by the 10 percent tolerance.

The proposal also clarifies that if the borrower requests a change in the type of loan, loan amount, or loan product, or otherwise makes a change to the mortgage transaction, the originator is not bound by the original GFE. However, because the borrower is in effect initiating a new application, today's proposed rule would require that the originator must either adhere to the original GFE or must redisclose to the borrower by providing a new GFE, and the originator would then be subject to the tolerances applicable to that GFE, provided the originator chooses to accommodate the change and the borrower qualifies for the change.

In addition, to meet the tolerances, today's proposed rule provides that originators must include all charges correctly within their prescribed category on the GFE (and the HUD–1/1A). This means that third party fees estimated on the GFE must be reported as the estimated prices to be paid to third parties only, and fees reported on the HUD–1/1A must not exceed those actually paid to third parties, except where the prices are based on an average calculated in accordance with proposed § 3500.8(b)(2). (See Section G discussion on average cost pricing in this preamble.)

While loan originators are expected to issue a GFE of settlement costs where a borrower submits a GFE application, in the case of new construction, settlement costs can change between the time a purchase contract is signed and settlement. Such estimates are subject to the provisions regarding unforeseeable circumstances and the provision for borrower requested changes, including the documentation requirements discussed below. The proposed rule provides that the loan originator may provide the GFE to the borrower with a clear and conspicuous disclosure stating that at any time up until 60 days prior to closing, the loan originator may issue a revised GFE. If no such disclosure is provided with the initial GFE, the loan originator would not be able to issue a revised GFE except as otherwise provided in the rule.

b. Unforeseeable Circumstances

The Proposed Rule. The proposal provides that loan originators should not be held to tolerances where actions by the borrower or circumstances concerning the borrower's particular transaction result in higher costs that could not have reasonably been foreseen at the time of the GFE application, or where other legitimate circumstances beyond the originator's control result in such higher costs. The proposal also provides that if unforeseeable circumstances result in a change in the borrower's eligibility for the specific loan terms identified in the GFE, the borrower must be notified of the rejection for the loan and be provided a new GFE if another loan is made available.

Discussion. While tolerances are necessary to provide ''bright line'' standards for consumers and industry alike, HUD recognizes that there may be circumstances under which loan originators should not be held to tolerances. The proposed rule details the circumstances under which tolerances may not apply, but indicates further that if it is possible for the loan originator to perform at all in such circumstances, the loan originator's charges may increase only to the extent caused by the particular circumstances.

Today's proposed rule defines ''unforeseeable circumstances'' as either: (1) Acts of God, war, disaster, or other type of emergency that makes it impossible or impracticable for the originator to perform; or (2) circumstances that could not be reasonably foreseen at the time of the GFE application, that are particular to the transaction and that result in increased costs, such as a change in the property purchase price, boundary disputes, or environmental problems that were not described to the loan originator in the GFE application; the need for a second appraisal; and flood insurance. As with any business transaction, the borrower has the ability to call off the transaction in such circumstances. The proposed rule specifically excludes market fluctuations from being regarded as unforeseeable circumstances.

Where an originator cannot perform or meet the tolerances because of unforeseeable circumstances, the originator must document the costs occasioned by the unforeseeable circumstances, and, as indicated, charge the borrower only the increased costs caused by such circumstances. Additionally, as indicated, when an increase in costs is necessary because of unforeseeable circumstances beyond the originator's control, the borrower should be notified within 3 days of such charges—as though a new application was filed—before any additional costs are incurred, and a new GFE reflecting the charges must be provided to the borrower. Finally, when unforeseeable circumstances result in a change in a borrower's eligibility for the loan identified in the GFE, the borrower should be notified within one business day of the decision to reject the loan, and, if another loan is made available to the borrower, a new GFE must be provided to the borrower. In all cases, the loan originator must retain appropriate documentation explaining any unforeseeable circumstances for a transaction for no less than 3 years after settlement.

9. Important Information for Borrowers

Page 4 of the GFE provides important information for the borrower, including information on how to apply for the loan set forth in the GFE. Page 4 also informs borrowers that they may wish to consult government publications about loans and settlement charges that have been published by HUD and the Federal Reserve Board. In addition, Page 4 provides important information to borrowers about their financial responsibilities as homeowners. This section of the GFE notifies the borrower that in addition to the monthly loan payment for principal, interest, and mortgage insurance, the borrower will be required to pay other annual charges to keep the property. The section provides the borrower with an estimate for annual property taxes, along with homeowner's flood, and other required property protection insurance, but estimates for other annual charges such as homeowner's association fees or condominium fees are not required to be provided on the form. The section informs the borrower that the borrower may have to identify such other charges and ask for additional estimates from other sources. The section also states that such charges will not change based on the loan originator chosen by the borrower and advises the borrower not to consider the loan originator's estimates of such charges, when shopping for the best loan.

Page 4 also notes that lenders can receive additional fees from other sources by selling the loan at some future date after settlement. However, the borrower is informed that once the loan is obtained at settlement, the loan terms, the borrower's adjusted origination charges, and total settlement charges cannot change.

Page 4 also includes a mortgage shopping chart that allows borrowers to compare GFEs from different loan originators.

10. Enforcement

The Proposed Rule. Today's proposed rule provides that charging a fee in excess of the tolerance, or any other failure to follow the GFE requirements, constitutes a violation of Section 5 of RESPA. As discussed below, HUD is also considering a provision that would allow loan originators a limited period of time to remedy any potential violations of the tolerances established under the rule, and thereby ease their possible exposure to liability for such violations.

Discussion. In enacting RESPA, Congress sought to protect consumers from unnecessarily high settlement charges. Accordingly, HUD believes that charging of a fee in excess of the tolerance, or other failure to follow the GFE requirements, constitutes a violation of Section 5 of RESPA.

HUD is soliciting comments on whether to add a provision to HUD's regulations that would allow loan originators, for a limited time after closing, to address the failure to comply with tolerances under HUD's GFE requirements, and if so, how such a provision should be structured. HUD is considering providing in the final rule that if, within a specified period (such as 14 business days) after the closing, a loan originator identifies a charge that exceeded the tolerance and repays the excess amount of the charge to the consumer within the specified period, the loan originator would be in compliance with Section 5. HUD is interested in commenters' views on whether such a procedure would be useful, and if so, what would be the appropriate time frame for finding and refunding excess charges. HUD is also soliciting comments on whether such a provision could be abused and therefore harmful to consumers, and whether the ability of prosecutors to exercise enforcement discretion obviates the need for such a provision.

F. Lender Payments to Mortgage Brokers—Yield Spread Premium (YSP)

Background. Lenders routinely provide the funds for mortgages that mortgage brokers originate for borrowers. Mortgage brokers also may be compensated for their services in originating the mortgage by the borrower and/or the lender. When the interest rate on the loan exceeds the par interest rate of the lender, the lender pays the broker at closing an amount in excess of the principal amount of the loan, and this excess is commonly referred to in the mortgage industry as a ''yield spread premium'' (YSP). For the past decade, such payments have been the subject of numerous lawsuits and consumer complaints, typically because consumers claim they were unaware that their broker was receiving such compensation, in addition to the direct compensation they paid the broker. Moreover, these consumers assert that such payments resulted from their being placed in mortgages with higher than necessary interest rates without their knowledge. Some consumer advocates have argued that all such payments should be treated as referral fees or kickbacks and thus should be illegal per se under RESPA.

HUD has taken the position, however, that YSPs can be useful and should remain available as an option for mortgage borrowers to help pay their closing costs, particularly those borrowers with limited available cash who choose to pay some or all closing costs through a higher interest rate. HUD made its position on the issue clear in HUD's Policy Statement 2001–1 (2001 Policy Statement).[16] In the 2001 Policy Statement, HUD restated its view [17] that as long as the broker's compensation is for services, and total compensation is reasonable, interest rate-based lender payments to the mortgage broker are legal under RESPA. HUD did not mandate new disclosure requirements in the 2001 Policy Statement, but did commit itself to making full use of its regulatory authority to establish clearer requirements for disclosure of mortgage broker fees, and to improve the settlement process for lenders, mortgage brokers, and consumers.[18] In the 2001 Policy Statement, HUD stressed that disclosure of broker compensation was ''extremely important and that many of the concerns expressed by borrowers over YSPs can be addressed by disclosing YSPs, borrower compensation to the broker, and the terms of the mortgage loan, so that the borrower may evaluate and choose among alternative loan options.'' [19] In brief, it has been HUD's consistent position that the existence of a YSP in any loan should be at the borrower's choice, based upon a complete understanding of the trade-off between up-front settlement costs and the interest rate.

HUD's current RESPA regulations require that a rate-based payment from a lender to a broker be reported on the GFE, and later on the HUD–1. Such payments are frequently characterized on the GFE and HUD–1 as a ''YSP'' or ''yield spread premium,'' and then are designated as a ''paid outside closing''

[16] Real Estate Settlement Procedures Act Statement of Policy 2001–1, Clarification of Statement of Policy 1999–1 Regarding Lender Payments to Mortgage Brokers, and Guidance Concerning Unearned Fees under Section 8(b), published October 18, 2001, at 66 FR 53052.

[17] 66 FR 53052.

[18] 66 FR 53052.

[19] 66 FR 53056.

or ''POC.''[20] The YSP is not often understood by the borrower. In addition, it is not listed as an expense to the borrower. At the same time, many brokers hold themselves out as shopping among various funding sources for the best loan for the borrower, and do not explain to the borrower that the payment they receive from the lender is derived from the borrower's interest rate. Some may even assert that the YSP is not a payment the borrower needs to be concerned with. The 2001 Policy Statement emphasized that earlier disclosure and the entry of yield spread premiums, as credits to borrowers would ''offer greater assurance that lender payments to mortgage brokers serve borrowers' best interests.''[21]

2002 Proposed Rule. The 2002 Proposed Rule provided that on the GFE, all brokers first disclose their total compensation charges and disclose any YSP as a lender payment to the borrower and discount points as additional borrower payments. The amounts of any lender payment or discount points would be combined with the total origination charges, to arrive at a net origination charge. It was this final figure that was to be emphasized and highlighted for borrower comparison among lenders and brokers.

The purpose of these changes in the GFE disclosure requirements, as proposed by the 2002 Proposed Rule, was to: (a) Make the borrower aware of the fact that the lender payments were a part of total origination costs, since they were directly related to the borrower's choice of a higher interest rate and monthly payment; (b) ensure that these payments worked to reduce out of pocket costs of the borrower; and (c) encourage the borrower to compare net origination costs of all loans whether from a lender or a broker, in order to select the loan product that best meets the borrower's needs. The rationale for the disclosure changes was to promote transparency, reduce borrower confusion, facilitate shopping, and, at the same time, avoid giving any competitive advantage to brokers or lenders in the marketplace.

Nearly all commenters on the 2002 Proposed Rule that discussed YSPs other than individual mortgage brokers or their national and state associations expressed support for greater broker fee disclosure. Consumer representatives, in particular, were strong supporters of disclosure along the lines that HUD proposed, and offered suggestions for making the requirements more enforceable. Consumer groups recounted the class action litigation that resulted from the payment of yield spread premiums and HUD's past statements committing the Department to ensuring better disclosure of yield spread premiums. The National Consumer Law Center (NCLC) said that to date, yield spread premiums are generally paid by the lender solely as compensation for a higher interest rate loan. In most cases, according to NCLC, the borrower is not only paying an up-front fee, but is also paying a higher interest rate as a result of being steered into above-par loans. Consumer groups asserted that the YSP should be defined for the consumer in simple, easy-to-understand language on the GFE.

Lenders and their trade groups, on the other hand, tended to favor HUD's requiring a separate Mortgage Broker Fee Agreement, as proposed by the lending industry in the last few years, which would be entered into by brokers and their customers, in addition to the GFE.

Mortgage brokers and their trade groups expressed vigorous opposition to disclosing the YSP as a credit to the borrower. They maintained that such a characterization is misleading, unfair, and anti-small business. The brokers stated that HUD's proposal: (1) Created confusion for the borrower; (2) would unnecessarily increase HOEPA transactions; (3) would stifle FHA and low/moderate-income lending; (4) would unfairly target brokers; (5) would create an uneven playing field with retail lenders; and (6) could adversely affect tax treatment of borrowers.

FHA Issue. Currently, FHA regulations limit origination fees for loans insured under the FHA program generally to one percent of the mortgage amount (see 24 CFR 203.27(a)(2)(i)). FHA does not have authority under the National Housing Act (12 U.S.C. 1709(b)(2)) to limit payments between loan originators, and yield spread premiums are not included in calculating the FHA limits on origination fees. Some industry commenters argued that the YSP disclosure, as proposed in 2002, would have adversely affected the origination of FHA loans. Specifically, the National Association of Mortgage Brokers (NAMB) commented that if the 2002 Proposed Rule were finalized, many mortgage brokers would cease to originate FHA loans because of the origination fee limitation. The MBA and some of its member firms argued for removal or adjustment of the FHA origination fee cap.

RESPA Roundtables. At the 2005 RESPA Reform Roundtables, consumer representatives generally continued to support disclosure of yield spread premium on the GFE. Mortgage broker representatives maintained their opposition to any yield spread premium disclosure on the GFE on the grounds that disclosure would put mortgage brokers at a competitive disadvantage as compared to lenders. Mortgage brokers also stated that if brokers are required to disclose yield spread premiums, lenders should also be required to disclose par, plus pricing, and gain on sales in the secondary market. Many lender representatives at the roundtables noted that it would be difficult for a lender to disclose any profit on a loan sold in the secondary market on the GFE, since the amount could not be ascertained with any certainty in advance, but in general, they did not express support for or opposition to a requirement for broker disclosure of the yield spread premium. Some participants at the roundtables, including consumer as well as industry representatives, recommended the use of a separate mortgage broker fee agreement in lieu of the yield spread premium disclosure requirement.

The Proposed Rule. Lender payments to mortgage brokers in table funded and intermediary transactions should be clearly disclosed to consumers on the GFE, and on the HUD–1 settlement statements as set forth below. The proposed rule would also streamline the current regulatory definition of ''mortgage broker.''

Discussion. For the past decade, HUD has required the disclosure of YSPs on the GFE and HUD–1 documents as a ''payment outside closing'' or ''POC.'' This means of disclosure proved to be of little use to consumers. Moreover, notwithstanding that lender payments to brokers are directly based on the rate of the borrower's loan, under current HUD guidance, such lender payments are not required to be included in the calculation of the broker's total charges for the transaction, nor are they clearly listed as an expense to the borrower. The confusion that can result when borrowers do not understand that mortgage brokers' total compensation includes lender payments derived from the interest rate is exacerbated by the fact that many brokers hold themselves out as shopping among various funding sources for the best loan for the borrower, while failing to explain to the borrower that the payment they receive from the lender is derived from the borrower's interest rate. On the other hand, some brokers tell their customers

[20] ''YSP POC'' sometimes appears on the second page of the HUD–1/1–A to represent ''Yield Spread Premium Paid Outside of Closing,'' which is rarely understood by borrowers as a payment they make out of their above-par interest rate.

[21] 66 FR 53056.

how they can use lender payments to lower the customer's up-front settlement costs.

The 2001 Policy Statement made clear that earlier disclosure and the entry of yield spread premiums as credits to borrowers would ''offer greater assurance that lender payments to mortgage brokers serve borrowers' best interests.'' [22] HUD could not mandate new disclosure requirements in the 2001 Policy Statement. HUD did, however, commit itself in the 2001 Policy Statement to making full use of its regulatory authority to establish clearer requirements for disclosure of mortgage broker fees, and to improve the settlement process for lenders, mortgage brokers, and consumers.[23]

It is for this reason that HUD proposed its new disclosure requirements in the July 2002 Proposed Rule. Having carefully considered the NAMB's and other comments in response to the 2002 proposal, as well as the comments presented at the RESPA Roundtables, and the results of consumer testing by the Federal Trade Commission (FTC) and HUD, as discussed below, HUD maintains that while YSPs to mortgage brokers must be clearly disclosed to borrowers, at the same time, mortgage brokers also must not be disadvantaged in the marketplace, since such disadvantage will only result in decreased competition and higher costs to consumers. Many mortgage brokers offer products that are competitive with and frequently lower priced than the products of retail lenders, as evidenced by brokers' large and growing share of the loan origination market, and HUD wishes to preserve continued competition and lower cost choices for consumers.

Today's proposed rule also streamlines the current regulatory definition of ''mortgage broker.'' Under the proposed definition, ''mortgage broker'' means a person (not an employee of the lender) or entity that renders origination services in a table funded or intermediary transaction. The definition would also apply to a loan correspondent approved under 24 CFR 202.8 for FHA programs.

The proposed definition would eliminate the current exclusion of an ''exclusive agent'' of a lender from the definition of ''mortgage broker.'' The current definition essentially excludes some persons who perform the same services as mortgage brokers as defined in 24 CFR 3500.2. In order to improve disclosure of settlement charges and increase transparency, HUD believes that all persons who perform mortgage broker services should be subject to the disclosure requirements. Therefore, an ''exclusive agent'' of a lender who is not an employee of the lender, but who renders origination services in a table funded or intermediary transaction, would be subject to the mortgage broker disclosure requirements set forth in this proposed rule.

HUD Research on Mortgage Broker Disclosures

1. *HUD's Testing of the GFE.* In October 2002, HUD contracted with a communication and consumer testing expert, Kleimann Communication Group, to revise and test the GFE and mortgage package forms,[24] in order to assure that the forms were user-friendly and enabled consumers to identify the least expensive loan. With respect to the GFE, the testing had the additional purpose of showing and explaining yield spread premiums and discount points to borrowers. New homebuyers and experienced homebuyers were part of the groups tested. The groups included members from diverse racial and ethnic groups, the elderly, and low-education and low-income groups. The testing of the GFE form was conducted in two phases.

2. *Phase 1 HUD Testing.* In Phase 1, the contractor conducted three rounds of one-on-one testing interviews to collect data about form comprehension and potential sources of confusion. The goal of the testing was to fine-tune and develop the GFE form and ensure that consumers can use the GFE in the way intended. Testing in this phase solicited consumer feedback through individual interviews with consumers as they actually used the GFEs in the simulated task of buying a home and needed to select between several loan offers. The data provide guidance about problems consumers have and the reasons for those problems. This phase consisted of three rounds of testing.

Each of the first two rounds of testing involved interviews with a total of 45 consumers in three cities. The contractor made several format and language changes to the form, as it was published in the July 2002, proposed rule, to improve readability and clarity. Among other changes, a summary page was developed and tested, with the specific charges for individual categories of settlement services appearing on a second page of the form. Kleimann then developed a comprehensive testing protocol that addressed the key objectives of the GFE form for consumers. The interviews with each participant lasted for 90 minutes with a 10-minute break. The interviews had two parts, one unstructured and one structured. In the unstructured portion of the interview, participants were asked to think aloud as they looked at each form for the first time. This unstructured and unprompted portion of the interview allowed Kleimann to capture users' initial reactions, including to areas that they responded well, to areas they did not understand, and to areas they questioned. The unstructured portion also ensured that the testers did not influence the comments of the participants by leading them to discuss information they would not have noticed on their own.

In the structured portion of the interview, Kleimann gave each consumer completed GFEs (as well as MPOs) and asked targeted questions to determine how well participants understood certain areas of the forms, whether the consumers could determine the least expensive loan, and how the forms might be improved. The study design focused on how the forms performed as stand-alone documents. The interviewer neither helped the participant understand any of the information on the forms nor answered any questions the participant asked to clarify information.

In these tests, 90 percent of participants chose the least expensive loan, when confronted with a choice between a GFE representing a loan from a lender (with no YSP shown) and a GFE representing a loan from a broker (with the YSP disclosed). The percentage increased slightly to 93 percent when an MPO was included as a third option.

Participants also understood the forms well. They could identify the basic loan costs and loan features. Over 90 percent could identify the total estimated settlement charges. The tested forms retained the trade-off table shown on the forms in the 2002 Proposed Rule, showing borrowers that if they wanted to receive a lower interest rate, they would have to pay more at settlement, and vice versa; 90 percent understood the trade-off table. About two-thirds of the participants could distinguish between items they, as consumers, could shop for and items for which they would use the broker's or lender's

[22] 66 FR 53056.

[23] 66 FR 53053.

[24] As noted in Section III above (Overview of HUD's Efforts Since 2002), the 2002 Proposed Rule included a ''guaranteed mortgage package agreement'' or ''GMPA,'' and HUD's contractor initially tested both the GFE and GMPA forms. In subsequent rounds of testing, the name of the GMPA form was changed to ''mortgage package offer'' or ''MPO'' and is referred to in this document as ''MPO.''

providers; almost two-thirds could explain the adjusted origination charge; and 70 percent of participants were able to identify the tolerances correctly in round 2 testing.

During the testing, Kleimann asked participants a number of questions about how they felt about the forms—how comfortable or uncomfortable they felt with the forms, what they liked and disliked, and how they perceived the information and the level of writing. Participants reacted very positively to the GFE layout and language, and to the clear delineation of charges. They found the summary page on page 1, the breakdown of charges on page 2, and the trade-off table on page 3 to be particularly useful. In round 2 of testing, 86 percent said the GFE had the right information for them, almost 90 percent said the GFE was written at the right level for them, and about two-thirds of participants said they were comfortable with the forms.

This testing was designed to see how the GFE form would perform as a stand-alone document. The interviewer neither coached nor led the participant by asking questions before the participant could work alone with the document. While this technique identifies how well participants use the GFE form as a stand-alone in a testing situation, consumers using these forms in the context of actual situations may perform even better. First, this testing involved no interaction at all between the potential borrower and a loan originator. In an actual situation, a loan originator would be able to answer borrower questions about the information on the forms and improve the borrower's understanding of it. Of course, some originators might try to confuse the borrower in order to collect higher fees, but a competitor might be more than willing to clear up that confusion, since doing so might get him the borrower's business. In addition to the help coming from the originator, borrowers could always ask someone else for help: A spouse, friend, their real estate agent, etc. Moreover, local consumer groups that focus on lending issues will also assist borrowers in understanding the new, streamlined GFE form. Since none of these sources were available during the testing, the Kleimann results should be viewed as underestimates of how much the new forms will help consumers once the forms are placed in an actual context of obtaining financing to purchase a home or refinance an existing loan. The third round of testing consisted of 60 participants, with 15 each in four cities, following the same procedures as in the first two rounds of testing.[25] The GFE form was changed in order to consider whether an alternative presentation of the discount points and yield spread premium, suggested by the National Association of Mortgage Brokers, would increase consumer understanding. The yield spread premium (YSP) and discount point disclosure was removed from the top of page 2, where it had been integrated into the calculation of total up-front charges to the borrower, and moved to page 3. As a consequence, page 2 included only the adjusted origination charge at the top. Thus, otherwise identical loans from a broker and a lender would have identical figures on page 2 as well as on page 1 of the summary. Page 3 contained the YSP and discount points. The form did not include a full calculation of total broker compensation, and thus differed from both the proposed rule and the first two rounds of testing.

The results showed that participants could continue to identify the cheapest loan: 93 percent of the participants correctly selected the broker loan as the cheaper loan as opposed to 90 percent in round 2. Also, in round 3 of testing, 89 percent of participants would have chosen the cheaper broker loan as opposed to 86 percent in round 2. None of the differences between these percentages in round 2 and round 3 is statistically significant. Also, as in the first two rounds, participants generally liked the form and would use it to comparison shop. They could identify the basic terms of the mortgage and the estimate of total settlement costs, and 86 percent understood the trade-off table. The material seemed to be presented at the right level and to be clearly laid out. Participants again identified the summary page, the breakdown of charges, and the trade-off table as useful.

However, participants had trouble understanding the concepts of YSP and discount points.[26] Only 3 percent and 30 percent, respectively, of the participants could paraphrase what YSPs and discount points represented, leaving over two-thirds of the participants unable to paraphrase. Participants did not understand how these two concepts (now located on page 3) related to other settlement charges (on page 2). Essentially, placing these terms outside the calculation of origination charges (that is, on page 3 instead of page 2 as in the first two testing rounds) seems to decrease participants' understanding of how the YSP and discount points fit into total loan costs. Since there was no significant improvement in participants' ability to determine the cheapest loan, and most participants did not understand the concept of YSP, HUD decided to keep the YSP on page 2 in the calculation in the 2005 Proposed Rule, as was the case in the 2002 Proposed Rule.

3. *FTC Testing.* During the same period that HUD was developing the revised GFE, FTC tested the effect of YSP disclosure to see if the disclosure had an adverse effect on the consumer's ability to comparison shop. Using a variation on the GFE form tested by Kleimann in round 2 testing, FTC extracted and tested a portion of the form. The first page of the extract consisted of an abbreviated version of the Summary Table from page 1 of the GFE. The second page of the extract contained the ''Your Charges for Loan Origination'' box and an abbreviated version of the ''Your Charges for All Other Settlement Services'' box from page 2 of the GFE. As a control, FTC took these same two extracts and eliminated the YSP and service charge, producing a second set of extracts. Thus, FTC isolated elements of the proposed GFE and created two variations of their extracts: with the YSP and without the YSP. FTC also tested the YSP disclosure from the GFE in HUD's 2002 Proposed Rule, and an alternative disclosure using language developed by FTC to describe the YSP and other loan terms.

FTC testers gave each participant a pair of loan extracts to evaluate: one had no YSP and thus represented a lender loan, and the other contained a YSP and thus represented a broker loan. The broker loan was $300 less than the lender loan. FTC asked participants which loan was cheaper and also which loan the participant would choose. Each participant also received a second set of extracts in which each loan offer was the same cost. The participants were asked the same two questions: which loan was cheaper and which loan would the participant choose.

FTC tested five groups with 103 or 104 participants per group. The results using the GFE variation of HUD's second round of testing are most relevant to the 2005 Proposed Rule. When the YSP was disclosed and the broker loan offer was cheaper, 72 percent of participants could correctly identify the broker loan as the cheaper loan; 17 percent incorrectly identified the lender loan as cheaper. Asked to identify which loan offer they would choose, 70 percent of participants

[25] The cities were Wilmington (Delaware), Tulsa, Minneapolis, and Los Angeles.

[26] These results are consistent with the work of Jackson and Berry (2001) and Woodward (2003a).

would have chosen the cheaper broker loan; and 16 percent would have chosen the lender loan. In contrast, when the form extract did not disclose the YSP, 90 percent correctly identified the broker loan as cheaper, and 85 percent would have chosen it. Disclosing the YSP caused an 18 percent drop in participants correctly identifying the cheaper loan and a 14 percent drop in the number who would choose it in the market. When costs of the broker and lender loans were the same on GFE forms that contained the YSP, participant performance decreased. Fifty-three percent reported that the loan costs were a tie; 30 percent believed the lender was cheaper; 11 percent believed the broker was cheaper. When asked to identify which loan offer they would choose, 25 percent of the participants chose either the lender or the broker loan offers; 46 percent selected the lender loan offer; and 17 percent selected the broker offer. In contrast, when the form omitted the YSP, 96 percent correctly identified the tie, and 78 percent chose one or the other as their preference.

FTC concluded that the YSP disclosure on the GFE form extract it tested had two drawbacks. First, its YSP disclosure impaired the ability of borrowers to comparison shop leading many to choose the more costly alternative. Second, the YSP disclosure introduced bias in the selection process that favored lenders over brokers. The Department's goal is to promote consumer shopping for mortgages and to prevent bias against any loan originator.

4. *Phase 2 HUD Testing.* FTC conducted its tests in February and March of 2003, and briefed HUD on the results during the summer of 2003. HUD decided to undertake additional testing and to incorporate the FTC test results in the further testing. For round 4 of testing, HUD asked Kleimann Communication Group to parallel aspects of the FTC study, including the questions asked, the difference between the amounts of each offer, and the length of the test situation.[27] HUD continued to test a full-length GFE rather than the portion tested by FTC, because HUD thought that the context of the entire form might provide a more accurate measure of participants' understanding of the GFE.

For round 4 of testing, 600 participants were selected; all received full GFEs. The control group received GFEs that omitted the YSP disclosure, while the experimental group received GFEs with the YSP disclosed. Each participant was given two pairs of loans: one in which the broker loan was $300 less than the lender and one in which the broker and lender loan offers were the same cost. Each participant was asked three questions for each set of GFEs: (1) Which offer was cheaper or if they cost the same, (2) which offer would they choose, and (3) why they made that choice. The results of this testing showed both consistency with and divergence from the FTC results.

When the YSP was disclosed, 83 percent of the participants correctly identified the broker loan as cheaper, and 8 percent incorrectly identified the lender as cheaper. These results were an improvement over the FTC results of 72 percent and 17 percent. In this GFE scenario, 72 percent of the participants said they would choose the broker offer and 11 percent said they would choose the lender. Similarly, in the FTC study, 70 percent of the participants chose the broker offer and 16 percent chose the lender offer.

When the YSP disclosure was removed, 92 percent correctly identified the broker loan as cheaper, and 1 percent incorrectly identified the lender as cheaper. These results are quite similar to FTC's results of 90 percent and 4 percent. When asked to choose a loan, 88 percent of participants chose the broker offer, while 1 percent chose the lender loan. These results compare to 85 percent and 3 percent respectively in the FTC testing.

When given same cost loan offers with a YSP, 81 percent correctly identified both loans as costing the same; 15 percent incorrectly identified the lender as cheaper; and 3 percent incorrectly identified the broker as cheaper. In contrast, in the FTC study, only 53 percent correctly identified the offers as costing the same; 30 percent incorrectly identified the lender as cheaper; and 11 percent incorrectly identified the broker as cheaper. In this GFE scenario, 50 percent of participants would have chosen either offer; 39 percent chose the lender offer; and only 5 percent chose the broker's. In contrast in the FTC study, only 25 percent chose either offer; 46 percent chose the lender offer; and 17 percent chose the broker's offer.

Of particular concern was the difference between participants who could identify the cheapest loan offer, but did not choose it. Analysis of the participant responses to the open-ended question of "why did you choose that offer" led to further modifications of the GFE to address this concern and to a fifth round of testing. In many comments, participants stated that they chose a particular offer because they did not want the "higher interest rate" indicated on page 2 of the GFE. They concluded from the language on the YSP disclosure that the interest rate was higher than the rate cited on page 1 under "Loan Details." Also, many of those who had no preference for the cheaper broker loan indicated that $300 was not a sufficient difference to be a deciding factor.

As a result of the testing and analysis, revisions were made to the GFE. First, the language in box 2 on page 2 of the GFE referring to the "higher interest rate" and "lower interest rate" was modified to reduce the possibility of borrowers" misinterpreting that the interest rate had changed from what was reported on the first page. Second, a third option was added to the YSP/discount points section on page 2 so a lender could indicate that its credits or charges were already included in "Our Service Charge." This addition was designed to ensure that participants would understand that a lender's origination charge might include a YSP or discount points, even though the YSP or points would not necessarily be known at the time of settlement, because the loan would not have been sold into the secondary market. The third option thus creates a closer parallel between broker and lender loans. Third, arrows were added on pages 1 and 2 to focus the borrower's attention on the subtotals and the total estimated charges, rather than on individual components. In addition, the typeface point size in the Total Estimated Settlement Charges on the bottom of page 1 was increased to further draw attention to the bottom-line.

For purposes of testing, three other changes were made to the GFEs. First, the difference in the total cost was changed to $500, to increase the likelihood that the difference would be a deciding factor. Second, another pair of loan options was added in which the lender offer was $500 less than the broker offer. This addition was intended to identify any bias for or against the broker and lender options. Finally, a set of four loans was added, to investigate whether the comparison across more than two offers increased or decreased participant performance. No version was tested without the YSP and discount points language.

[27] Kleimann's report, entitled *Consumer Testing Results for HUD's Good Faith Estimate (GFE) Form: Rounds 4 & 5* (dated March 19, 2004), provides information on the specific characteristics of the consumers tested, revisions that Kleimann made to the form and the reasons for those revisions, the specific cities where the tests were conducted, the testing protocols, testing conditions, and the main results from each round of testing.

For round 5 of testing, 600 participants were divided into two groups, both of which received the revised GFE.[28] The first group received the revised GFE with changed language and with the addition of a third option so that lenders could indicate that YSP and discount points had been included in ''Our Service Charge.'' The second group received the identical revised GFE, but the third option box was removed. All participants received three pairs of loans, one with the broker offer being lower by $500, one with the lender offer being lower by $500, and one in which both offers were the same. In addition, each participant received a set of four offers to compare.

The three option GFE and the two option GFE performed quite similarly with the three option form consistently getting slightly better results. The proposed rule therefore discusses only the three option form, and that form is included in the proposed rule.

In the GFE in which the broker was cheaper, 92 percent of the participants correctly identified the broker as the cheaper loan offer. This result represents an improvement over the 72 percent reported by the FTC study and the 83 percent reported in the round 4 results. Only 3 percent of the participants incorrectly identified the lender as the cheaper loan offer, compared to the 17 percent reported by the FTC and 8 percent in round 4. When asked to choose a loan, 87 percent of the participants chose the cheaper broker loan as compared to 70 percent of the participants in the FTC study and 72 percent of the participants in round 4. These results of round 5 of testing are significantly better than the FTC's results and are based on a much larger sample.

In the GFE in which the lender was cheaper, 92 percent of the participants correctly identified the lender as the cheaper loan offer. Only 1 percent incorrectly identified the broker as cheaper. When asked to choose a loan, 89 percent of the participants chose the lender loan and less than 1 percent chose the broker.

The purpose of testing the case in which the lender was cheaper than the broker was to test for bias by seeing if the GFE forms performed equally well when either the lender or broker was the cheaper loan. A comparison of the results indicates that there is no bias against brokers when the loans have different borrower costs.

In the GFE in which the broker and lender loan offers were of equal cost, 90 percent of the participants were able to correctly identify that fact. This result compares very favorably with the 53 percent reported by FTC and the 81 percent from round 4 of testing. Participants in round 5 misidentified the lender as cheaper seven percent of the time, compared to 30 percent in the FTC results and 15 percent in round four. Participants misidentified the broker as cheaper 1 percent of the time as compared to 11 percent in the FTC study and 3 percent in round 4. Participants said they would choose either loan 70 percent of the time, a dramatic increase over the 25 percent in the FTC study and the 50 percent in round four. Twenty-one percent would choose the lender as compared to 46 percent in the FTC study and 40 percent in round 4. Four percent of participants chose the broker compared to 17 percent in the FTC study and 5 percent in round 4 of testing.

To further test whether increased context improved or decreased consumer performance with the revised GFE, the Department asked Kleimann to give the participants a four-loan comparison as well. For this four-way comparison, HUD included a blank worksheet or shopping chart to aid participants in comparing the loans, as page 4 of the GFE form. The worksheet contained spaces for the originator's name, loan amount, interest rate, term, monthly payment, adjusted origination charge, charges for all other settlement services, and total estimated settlement charges. On page 1 of the GFE, a sentence telling participants to use the table to compare offers was inserted. Additionally, half of the participants were given explicit verbal directions to use the worksheet.

The 300 participants who had received the three option GFE were included in this four-way comparison. Half were given a set in which a broker loan offer was the cheapest. The other half were given a set in which a lender and a broker loan offer cost exactly the same and were the cheapest at $6,500. Only 150 participants received explicit verbal instructions to use the worksheet in their comparison, while half received no instructions.

In the comparison in which a broker loan offer was the cheapest, 92 percent of participants who were not verbally reminded to use the comparison worksheet correctly reported the broker loan as the cheapest. Very few of the participants who were not verbally reminded to use the comparison worksheet used it. When instructed to use the comparison sheet, many participants did, and 97 percent correctly identified the broker loan as the cheapest. The overall success rate for correctly identifying the correct loan as the cheapest for both those getting and those not getting the verbal instructions to use the comparison worksheet was 95 percent, with only 1 percent misidentifying a lender loan as cheaper.

In the case where both loans cost the same and no verbal instructions were given to use the comparison sheet, 41 percent picked the broker loan as cheaper and 49 percent picked the lender loan. With verbal instructions to use the worksheet, 57 percent picked the broker at $6,500 and 35 percent picked the lender at $6,500. The combined average was 49 percent for the broker and 41 percent for the lender. There was no bias against the broker when costs were the same.

5. *Sixth Round of Testing.* HUD conducted a sixth round of consumer testing in November 2007. The testing consisted primarily of qualitative tests of the GFE and an introductory qualitative test of the closing script (referred to in testing as ''the summary''). Compared to previous rounds of testing, the testers found that participants were more aware, due to recent intensive media coverage of mortgage market difficulties, personal experience, and the experiences of relatives and friends, of the issues facing a consumer choosing a mortgage loan. The modifications to the GFE for round 6 included an expanded disclosure of loan terms on page 1 of the GFE, clarifying language regarding the important dates when actions must be taken by the consumer, changes in the title and description of government recording and transfer charges, and new language regarding additional compensation lenders may receive after closing for selling the loan.

Consumers appreciated the enhanced loan terms disclosures designed to alert the borrower to potentially unfavorable changes in their obligations during the term of their loans. Participants stated that they liked the form length, the language of the GFE, and the layout of pages 1 and 2. Participants appreciated the trade-off table on page 3 and used it to compare loans. As a result of the round six testing, information on the existence of an escrow account was added in the ''Summary of your loan terms'' section on page 1, and a section entitled ''Your financial responsibilities as a homeowner'' was added at the top of page 4. Finally, the tolerance presentation was changed from a pure list of headings and bullets on page 3,

[28] Participants were chosen for demographic diversity in the same five cities: Atlanta, Boston, Denver, Seattle, and Tulsa. No participant from round 4 was permitted to participate in round 5.

to bullets within columns according to the tolerance that applies.

Testers conducted settlement/closing simulations to test the idea of the closing script. Participants thought the loan details were clear and understandable and reacted positively to having the summary read aloud. Participants were more attentive to loan details, were more aware of the tolerance categories and how they related to charges, and were better able to identify tolerance violations when the script was read aloud than when they reviewed the script documents independently.

Revisions to the GFE Based on Testing

The GFE form proposed today is the result of an iterative testing process comprised of six rounds of consumer testing of the form during the 2003–2007 period. HUD's testing contractor used the data collected from testing participants during each round to improve and modify the form throughout the testing process. A summary report with detailed information on each round of testing is available at *http://www.huduser.org/publications/hsgfin/GoodFaith.html*. Based on this testing, HUD has made revisions in the GFE disclosure form and now presents the net origination charge on the first page of the form as ''your adjusted origination charges.'' This amount is added to the charges for all other services to arrive at the total estimated settlement charges for the mortgage on the first page. This new approach to disclosure helps consumers focus appropriately on the net charges of the originator when comparing similar loans, from either a lender or a broker, and on the total estimated settlement charges. The fourth page of the form provides a Mortgage Shopping Chart that also helps borrowers compare total charges for various mortgage loans.

The second page of the new GFE informs the consumer how the adjusted origination charge is computed. Block 1 discloses as ''Our service charge'' the originator's total charge to the borrower for the loan. (The form no longer refers to this total charge in Block 1 as ''maximum'' compensation.)

Today's proposed rule proposes to require that in the case of loans originated by mortgage brokers, the amount in Block 1 must include all charges received by the broker and any other originator for, or as a result of, the mortgage loan origination, including any payments from the lender to the broker for the origination. In the case of loans originated by originators other than mortgage brokers, the amount in Block 1 must include all charges to be paid by the borrower that are to be received by the originator for, or as a result of, the loan origination to the borrower, except any amounts denominated by the lender as discount points or amounts that the lender chooses to call a credit and which are disclosed in Block 2.

Block 2 discloses for loans originated by mortgage brokers whether there is any charge or a credit to the borrower for the specific interest rate chosen for the GFE. The second check box indicates whether there is a payment for a higher interest rate loan described, as the ''credit of $____ for this interest rate of __%. This credit reduces your upfront charges.'' The third check box indicates any ''charge of $____ for the interest rate of __%. This payment (discount points) increases your upfront charges.'' Any lender payment is then subtracted and any points are added to arrive at ''your adjusted origination charge'' that is also disclosed on the first page of the form. For mortgage brokers, the amounts of any charge or credit in Block 2 must equal the difference between the price the wholesale lender pays the broker for the loan and the initial loan amount.

At page 2, while lenders are not required to check the second or third boxes of Block 2, in loans where they do not make such disclosures, they are required to check box 1 that indicates that ''The credit or charge for the interest rate chosen is included in the service charge.'' If lenders denominate any amounts due from the borrower as ''discount points,'' they must check the third box indicating that there are charges for the interest rate and enter the appropriate amount for points as a positive number. If lenders denominate any amounts as a credit to the borrower for the particular interest rate covered by the GFE, they must check the second box and enter the appropriate amount as a negative number. Lenders must also add any such positive amounts or deduct any negative amounts to arrive at ''Your Adjusted Origination Charge,'' which is also to be disclosed on page 1 of the form.

Considering that mortgage brokers are required to disclose payments from lenders while lenders are not required to disclose payments they receive from the secondary market, by virtue of the ''secondary market exemption,''[29] HUD considered providing only the adjusted origination charge and disclosing the YSP and discount points elsewhere on the form without the calculation. HUD concluded, however, that a complete disclosure of payments to the broker as presented on page 2 of the form, read in conjunction with the chart on page 3 of the form, was essential to borrower understanding of: (1) The broker's total compensation; (2) how rate-based payments from lenders can help reduce borrowers' up-front origination charges and settlement costs in brokered loans; and (3) how payments to reduce the interest rate and monthly payment increase up-front charges. Because mortgage broker compensation occurs at settlement and can be readily ascertained, full disclosure of total broker compensation is appropriate. On the other hand, even in the absence of the secondary market exemption, a similar disclosure of lender compensation would not be appropriate because it is difficult to measure secondary market payments with any precision at the time of settlement and because a lender may or may not choose to sell a particular loan at some point in the future. However, the GFE form includes a notation on page 4 that lenders may also receive an additional payment if they sell the loan after settlement.

Furthermore, based on testing by HUD's contractor, as discussed above, the YSP disclosure without an explanation of its context was not useful to consumers. On the other hand, based on testing, by moving to a form that requires in Block 2 that lenders disclose that credits or charges may be included in their service charge as well, even when the calculation is on the form for brokered loans, borrowers are not confused and correctly compare adjusted origination charges between loans from mortgage brokers and loans from lenders even when the YSP is included in the calculation of the adjusted origination charge. Nevertheless, to help borrowers identify the lowest-cost loan without being confused by the presence of a YSP, HUD established the first page of the form as a summary page that only includes adjusted origination charges, moved the ''calculation'' of any credit (YSP) or charge to the second page of the new GFE, and then established the new Mortgage Shopping Chart at page 4 to facilitate comparison shopping. HUD is now convinced that by making these changes, any disadvantage to brokers is virtually eliminated. Also, consistent with the FTC's 2002 comment, HUD proposes to include in the revised Special Information Booklet advice to borrowers that lenders also may receive payments from financial institutions when they sell the mortgage but are not

[29] As set forth in 24 CFR 3500.5(b)(7), a bona fide transfer of a loan obligation in the secondary market is not covered by RESPA and this part, except as set forth in section 6 of RESPA (12 U.S.C. 2605) and 24 CFR 3500.21.

required to disclose such payments and, for this reason, borrowers should focus on net origination charges of loan originators for comparable mortgages.

To avoid borrower confusion, the term ''lender payment to the borrower'' that had been included in the 2002 Proposed Rule also has been dropped. Through its use of this term in the earlier proposal, HUD had sought to have borrowers focus on the payment, and understand that it was a consequence of their choice of rate. HUD now recognizes the original terminology warranted improvement.

In arriving at changes in the proposed revised GFE form, HUD also considered the possibility of adopting the Mortgage Broker Fee Agreement developed by representatives of the lending and brokerage industries. These forms disclose the total amount of fees to the broker and explain that the fees may include lender payments, but not the specific amount of such payments. HUD believes, however, that it is better for the borrower to understand the lender payment and its relationship to higher interest rates so that he or she can use the payment to lower his or her up-front costs, rather than simply to disclose the possibility of such payment to the borrower. For these reasons, HUD remains committed to improving the GFE disclosure rather than requiring yet another new form or agreement.

In its consultations with staff of the Federal Reserve, HUD raised the concern expressed by some commenters that treating lender payments to mortgage brokers as a credit toward the origination charges could increase the points and fees of each brokered mortgage loan, resulting in more loans coming under HOEPA coverage. Federal Reserve staff advised HUD that, notwithstanding HUD's changed requirements, determinations of whether payments to a mortgage broker must be included in the finance charge and whether a loan is covered by HOEPA are based on the statutory definitions and requirements in TILA as implemented by the Board's Regulation Z, which are unaffected by HUD's RESPA rulemaking.

HUD also recognizes that many loan originators today offer loans with no up-front fees due from the borrower. These loans have become more popular over the years. The proposed GFE can easily accommodate these ''no cost'' loans. In the case where ''no cost'' means no up-front payment to the loan originator, the figure in Block A equals zero. This implies that any credit identified in Block 2 would exactly offset the charge in Block 1. While a mortgage broker would always be required to enter the actual amount of any yield spread premium in Block 2, a lender could alternatively enter zero for the credit, in which case the charge in Block 1 would also have to equal zero so that the combination to be reported in Block A would equal zero.

Alternatively, the borrower might want to pay a lower interest rate and monthly payment than that associated with a ''no cost'' loan. The borrower generally may do this by buying the interest rate down. This is done by paying an up-front fee to the loan originator that compensates the loan originator for the lower interest rate and monthly payments it will receive over the life of the loan. The more the borrower pays, the lower the interest rate and monthly payments will be. The amount the borrower pays to buy the rate down shows up in Block A as a positive number. This would result from a higher value in Block 1 or a higher value in Block 2. (A lower credit in Block 2 or a higher charge in Block 2 yields a higher value in Block 2, and in Block A as well.) Thus, either ''no cost'' loans or those where the borrower buys down the interest rate can be accommodated on the proposed GFE. In the first case, the value in Block A is zero. In the second, Block A represents what is paid to buy the interest rate down.

In the case where ''no cost'' encompasses some third party fees as well as the up-front payment to the loan originator, the figure in Block A would have to be a negative value large enough to offset the third party fees covered under this definition of ''no cost.'' For brokers, who are required to report yield spread premiums, this implies that the yield spread premium identified in Block 2 as a credit would be larger than the charge in Block 1. The sum of the positive value in Block 1 and the negative value, the credit, in Block 2 would equal a negative value large enough to offset the third party fees. Lenders are not required to report yield spread premiums. But they are permitted to enter credits in Block 2. If a lender chooses to do so, then the yield spread premium identified in Block 2 as a credit would have to be larger than the charge in Block 1. Just as in the broker case, the sum of the two would equal a negative value large enough to offset the third party fees for a ''no cost'' loan. Finally, today's proposed rule states that loan originators must include all charges correctly within their prescribed category on the GFE and the HUD–1 (or HUD–1A). The amounts for categories involving third parties can include only amounts paid to the third party, and must not include amounts retained by the loan originator for related services performed by the loan originator. The amount charged to the borrower and shown on the HUD–1 in an individual transaction may be based on an average calculated in accordance with proposed § 3500.8(b)(2). (See Section E discussion on average cost pricing.) HUD believes these rules are required to assure that, pursuant to Sections 4 and 5 of RESPA, originators provide borrowers accurate disclosures of settlement charges on the GFE, HUD–1, and HUD–1A.

FHA Limit. Under its current regulations, HUD places specific limits on the amount a mortgagee may collect from a mortgagor to compensate a mortgagee for expenses incurred in originating and closing a FHA-insured mortgage loan (see 24 CFR 203.27).[30] In light of the considerations below and its proposed changes to the HUD–1/1A, HUD is today proposing a change to the FHA regulations limiting origination fees of mortgagees. FHA considered deregulating the loan origination fee limitation in 1988 (see 53 FR 15408, April 28, 1988), but did not pursue a final rule at that time.

HUD believes that its RESPA policy statements on lender payments to mortgage brokers restrict the total origination charges for mortgages, including FHA mortgages, to reasonable compensation for goods, facilities, or services. [31] While the FHA limit on origination fees only regulates fees from mortgagors to mortgagees and does not include any payments between mortgagees, HUD is aware that in recent years mortgage brokers have routinely utilized yield spread premiums in FHA mortgage transactions to supplement their compensation beyond the amount they receive directly from the borrower. Studies by HUD confirm this.

HUD believes that improvements to the disclosure requirements for all loans sought to be achieved as a result of the rulemaking should make total loan charges more transparent and allow market forces to lower these charges for all borrowers, including FHA borrowers. Therefore, HUD is proposing in this

[30] Under 24 CFR 203.27(a)(2)(i), origination fees are limited to one percent of the mortgage amount. For new construction involving construction advances, that charge may be increased to a maximum of 2.5 percent of the original principal amount of the mortgage to compensate the mortgagee for necessary inspections and administrative costs connected with making construction advances. For mortgages on properties requiring repair or rehabilitation, mortgagor charges may be assessed at a maximum of 2.5 percent of the mortgage attributable to the repair or rehabilitation, plus one percent on the balance of the mortgage. (See 24 CFR 203.27(a)(2)(ii) and (iii).)

[31] See Statement of Policy 1999–1, 64 FR 10080, March 1, 1999, and Statement of Policy 2001–1, 66 FR 53052, October 18, 2001.

rulemaking to remove the current specific limitations on the amounts mortgagees presently are allowed to charge borrowers directly for originating and closing an FHA loan. The FHA Commissioner would retain authority to set limits on the amount of any fees that mortgagees charge borrowers directly for obtaining an FHA loan.

The proposed rule would also permit other government program charges to be disclosed on the blank lines in Section 800 of the HUD–1/1A.

G. Modification of the HUD–1 Settlement Statement

The Proposed Rule. The current HUD–1/1A Settlement Statements would be modified to allow the borrower to easily compare specific charges at closing with the estimated charges listed on the GFE. In addition, an addendum would be added to the HUD–1/1A that would compare the loan terms and settlement charges estimated on the GFE to the final charges on the HUD–1 and would describe in detail the loan terms for the specific mortgage loan and related settlement information. The settlement agent would be required to read the addendum aloud to the borrower at settlement and provide a copy of it at settlement.

Discussion. As recommended at the 2005 RESPA Roundtables, HUD is today proposing to modify the HUD–1/1A form to make it comparable to the GFE. The HUD–1 is well accepted as a listing of settlement service charges by industry and consumers alike. However, there is a risk that if a borrower cannot easily compare the estimated charges listed on the GFE with the settlement charges listed on the HUD–1/1A, a settlement service provider could deviate from the prices listed on the GFE and the borrower would not realize such deviation prior to closing. Thus, borrowers would not be able to fully realize the financial savings that will result from comprehensive RESPA reform. Many participants at the RESPA Reform Roundtables recommended that in order to ensure the maximum cost savings to borrowers, the GFE and the HUD–1 should be easily comparable so that borrowers will be able to compare the estimated costs with the actual costs at closing. While some participants recommended that a new GFE be designed to correspond to the HUD–1, others recommended that the HUD–1 be redesigned to correspond to a new GFE that includes major cost categories.

HUD recognizes that the HUD–1/1A forms are the most widely used and accepted forms in the mortgage industry and does not undertake changes to these forms lightly. However, because HUD believes that the GFE and the HUD–1 should be easily comparable, today's proposal sets forth changes to the HUD–1/1A that will allow borrowers to easily compare the figures on the GFE to the final charges at settlement. The proposed changes facilitate comparison of the two documents by inserting, on the relevant lines of the HUD–1/1A, a reference to the corresponding block on the GFE. With such changes, a borrower would be able to easily compare a figure in a particular column on the HUD–1/1A with the corresponding figure on the GFE. In addition, creating new labels for lines, showing totals while still permitting disclosure of details so long as not shown in either column or paid outside closing (POC), and leaving blank lines allows the HUD–1 to still function as an effective settlement document.

The instructions for completing the HUD–1 will clarify the extent to which charges for individual services must be itemized. In general, the HUD–1 must separately itemize every service provided by a third party (i.e., other than the loan originator) to show the name of the party ultimately receiving the payment, along with the total amount received. However, services connected to the origination of the loan must not be separately itemized, even if a loan originator uses a third party to perform those services. For example, charges for document handling or processing should not be separately itemized, but instead should be included in the loan originator's own charge, since those types of services are ordinarily performed by the loan originator itself. Today's proposed rule adds a definition of ''origination services'' to clarify the types of services that may not be separately itemized on the HUD–1.

The instructions for completing the HUD–1 also clarify the extent to which charges for title services must be itemized. In general, the HUD–1 must separately identify each service provider that is performing title services, along with the total amount received. If a party other than the title company listed on line 1101 of the HUD–1 provides services that are separate from providing title insurance, such as attorney and settlement or escrow agent services, the title company should separately itemize those services with the total amount paid to that provider, to the left of the columns. However, charges for services defined as ''primary title services'' such as abstract, binder, copying, document handling, or notary fees, should not be separately itemized on the HUD–1, even if a party other than the title company listed on line 1101 of the HUD–1 provides those services.

Today's proposed GFE distinguishes between those settlement costs attributable to the loan originator and charges for all other settlement services. However, Section 800 of the current HUD–1/1A forms combines loan originator costs and some third party costs under the same heading (''Items Payable in Connection with Loan''). In order to facilitate comparison between the GFE and the HUD–1/1A for this section, the proposed HUD–1 replaces the existing line descriptions on the current HUD–1/1A with the relevant headings from the GFE. Thus, Line 801 on the proposed HUD–1 lists ''Our service charge (from GFE #1)'' to refer back to Block 1 on the GFE. In lieu of the ''Loan discount'' terminology on the current Line 802 of the HUD–1/1A, the proposed Line 802 includes ''Your charge or credit for the specific interest rate chosen (from GFE #2)'' to refer back to Block 2 on the GFE. Line 803 of the proposed HUD–1/1A lists ''Your Adjusted Origination Charges (from GFE Block A)'' and corresponds to GFE Block A. Lines 804 to 807 on the proposed HUD–1/1A for appraisal fee, credit report, tax service, and flood certification include notations indicating that the charges are listed in Block 3 on the GFE (required services selected by the loan originator). The dollar value showing up in GFE Block A can show up as POC, in the borrower's column, or in the seller's column. On line 803, the sum of the figures labeled as POC, in the borrower's column and in the seller's column should be compared to the figure in GFE Block A. The figures on Blocks 1 and 2 of the GFE must not show up in either column or as POC in order to avoid double-counting.

For Section 900, ''Items Required by Lender to be Paid in Advance,'' Line 901 of the proposed HUD–1/1A lists ''Daily Interest Charges (from GFE #8)''; Line 902 lists ''Mortgage insurance premium (from GFE #3 or #5);'' and Line 903 lists ''Homeowner's insurance (from GFE #9).''

For Section 1000, ''Reserves Deposited with Lender,'' the proposed HUD–1/1A inserts Line 1001 ''Reserves or escrow (from GFE #7)'' and then renumbers the current lines. For Section 1100, ''Title Charges,'' the proposed form inserts Line 1101 ''Title services and lender's title insurance (from GFE #4)'' and then renumbers the current lines. Line 1110 lists ''Optional owner's title insurance (from GFE #10).''

For Section 1200 ''Government Recording and Transfer Charges,'' the proposed HUD–1/1A inserts Line 1201, ''Government Recording and Transfer Charges (from GFE #6)'' and renumbers current lines. For Section 1300 ''Additional Settlement Charges,'' Line 1301 includes ''Survey (from GFE #5)''and Line 1302 ''Pest inspection (from GFE #5).''

The figures from Blocks 3 and 5 on the GFE are broken out and listed individually on the HUD–1 in the columns or as POC. The totals are not listed as POC or in the columns to avoid double-counting.

All items on the HUD–1/1A that correspond to an item on the GFE are made to stand out by using a different font from the other text on the HUD–1, such as by bolding the text or using italics, so it is easier for the borrower to find these numbers when comparing the forms.

Addendum to the HUD–1/1A, ''Closing Script.'' In addition to the proposed changes to the HUD–1/1A discussed above, HUD is proposing an addendum to the HUD–1 that would be provided to the borrower at closing. The loan originator would transmit to the settlement agent all information necessary to complete the prescribed addendum to the HUD–1/1A settlement form, referred to as the ''closing script.'' The addendum would be prepared by the settlement agent and would have to accurately reflect the loan documents and related settlement information provided by the lender. The settlement agent would be required to read the addendum aloud to the borrower at settlement. The addendum would compare the loan terms and settlement charges estimated on the GFE with those on the HUD–1 and would describe in detail the loan terms for the specific mortgage loan as stated in the mortgage note, and related settlement information. The length of the addendum would vary depending on the specifics of the borrower's loan.

HUD is proposing the addendum to address the frequent complaints it receives from borrowers that the costs quoted at the GFE stage varied considerably from the costs imposed at settlement. In addition, HUD continues to receive complaints from borrowers indicating that they were unaware or unsure of the terms of the loan provided at settlement. HUD believes that by making borrowers aware of their loan terms at the settlement, many problems after settlement can be avoided.

HUD believes that greater borrower awareness and understanding of the settlement charges will help prevent the imposition of charges at settlement that were not included at the GFE stage. By reviewing each charge with the borrower at settlement, the closing agent will be able to highlight those charges that may have changed between the GFE stage and the settlement. In this fashion, the borrower will be able to more easily question any charges at the settlement, rather than after the settlement, when it becomes more difficult to address the issue or provide borrower satisfaction. HUD believes that the addendum to the HUD–1 complements the proposed GFE by apprising the borrower as to whether the tolerances imposed by the proposed GFE have been met, thereby minimizing post-settlement questions as to any cost variances between the GFE and the HUD–1.

With respect to issues arising from the loan provided at settlement, the most frequent complaints stem from the following: The interest rate for the loan the borrower received was not the interest rate applied for; the borrower applied for a fixed rate loan but received an adjustable rate loan at settlement; and the closing documents were not explained to the borrower, leaving the borrower unaware or unsure of important loan information. In addition, HUD is aware that in many cases, borrowers are unaware of or confused by certain loan terms. This problem has become more acute with the rise of non-traditional mortgages. For example, many borrowers do not have a solid understanding of negative amortization or are unaware of the potential for negative amortization. For borrowers with adjustable rate loans, many do not understand the maximum amount their monthly mortgage payment could reach when the interest rate adjusts. In addition, many borrowers are unaware of the prepayment penalty in their loan until they try to refinance.

To address these issues, today's proposed rule would require the settlement agent or other person conducting the settlement to read the closing script document aloud to the borrower and explain: (1) The comparison between the loan terms and the settlement charges listed on the HUD–1/1A settlement form with the estimate of charges listed on the GFE; (2) whether or not the tolerances have been met; and (3) the loan terms, as contained in the mortgage note and related settlement information. Any inconsistencies between the mortgage note, between related settlement information and the GFE, and between the HUD–1/1A settlement charges and the GFE would have to be disclosed and explained to the borrower. The proposed rule would also require that the closing script addendum be delivered to the borrower as part of the HUD–1/1A at the closing. Upon request of the borrower, the HUD–1/1A and the closing script addendum would have to be made available for review by the borrower 24 hours prior to the settlement, in accordance with 24 CFR 3500.10.

The instructions to the preparer of the closing script are included in Appendix A to the rule. Examples of closing scripts are also provided in Appendix A to the rule. All instructions for completing the closing script are proposed to be codified with the rule at the final rule stage.

Enforcement. The Proposed Rule. The proposed rule provides that failure to complete the HUD–1 in accordance with the regulations constitutes a violation of Section 4 of RESPA.

H. Permissibility of Average Cost Pricing and Negotiated Discounts

The Proposed Rule. The proposed rule would recognize pricing mechanisms that result in greater competition and lower costs to consumers, specifically average cost pricing and some discounts among settlement service providers, including volume-based discounts. The proposed rule would amend 24 CFR 3500.8 and would explain that charges for third party services may be calculated using average cost pricing mechanisms based on appropriate methods established by HUD. These mechanisms would also accommodate certain volume-based discounts. Although the third party charge on any one loan may be higher than the average, the third party charge on another loan may be lower, provided that borrowers are being charged no more than the average price actually received by the third parties during the period on which the average price is computed. The proposed rule would allow loan originators to disclose on the HUD–1 an average cost price in accordance with one of several specific methods. The proposed rule would also amend 24 CFR 3500.14(d) and the definition of ''thing of value'' to clarify that it is permissible for settlement service providers to negotiate discounts in the prices for settlement services, so long as the borrower is not charged more than the discounted price. The practice of negotiating discounts in prices—whether among settlement service providers, such as with volume-based discounts, or by a settlement service provider on behalf of consumers—can serve to reduce prices to consumers.

Discussion. In this proposed rule, HUD is seeking to facilitate pricing arrangements that will benefit consumers. HUD has determined that in the evolving marketplace, certain loan originators and third party settlement service providers may wish to adopt average cost pricing and to offer discounts, including volume-based discounts. HUD welcomes comment on these and any other pricing techniques that may result in greater competition and lower costs to consumers and that are consistent with the purposes of RESPA.

Congress authorized the Secretary, pursuant to Section 19(a) of RESPA, to prescribe such rules and regulations and to make such interpretations as may be necessary to achieve the purposes of RESPA. In enacting RESPA, Congress found that reforms in the real estate settlement process were needed to protect consumers from the unnecessarily high settlement charges that had evolved in some areas of the country. Congress explained the purpose of RESPA as being to effect changes in the residential settlement process that will result ''in more effective advance disclosure to home buyers and sellers of settlement costs'' and ''the elimination of kickbacks or referral fees that tend to increase unnecessarily the costs of certain settlement services.''

Congress sought to achieve its purposes through both prohibitions on conduct and better consumer disclosures. The Senate Committee Report on S.3164, the bill that was eventually enacted as RESPA, noted that the Committee on Housing, Banking, and Urban Affairs recommended an approach to the problems of settlement costs that would regulate the underlying business relationships and procedures of which the costs are a function, rather than regulating closing costs directly. (See S Rep. 93–866, at 3 (1974).) Through the prohibitions against kickbacks and unearned fees in Section 8 and the escrow account requirements in Section 10, the Senate Committee was aiming to ensure that the costs of buying a home would not be ''unreasonably or unnecessarily inflated'' (Id). In fact, the Committee expected that advance disclosure of settlement charges would reduce or eliminate many ''unnecessary or unreasonably high settlement charges'' (Id).

Section 4(a) of RESPA authorizes the Secretary to prescribe the primary disclosure document for settlement, the Uniform Settlement Statement, generally known as the HUD–1 (or HUD–1A) Settlement Statement. This standard form is used at settlement to disclose all charges imposed on the borrower and the seller. Section 4 is silent, however, on how such charges are calculated. Congress expressly encouraged flexibility on the application of at least some of the Section 4 requirements relating to the HUD–1 Settlement Statement, by allowing for the deletion from the form of items that are not required by local custom.

In Section 5(c) of RESPA, Congress required that the lender provide to the borrower ''a good faith estimate of the amount or range of charges'' that the borrower is likely to incur at settlement. Section 5, like Section 4, is silent on how such charges are to be calculated. This GFE of charges is to be included with a special information booklet that contains information about the homebuying and home finance process. Section 5(b)(1) of RESPA requires that the booklet include ''a description and explanation of the nature and purpose of each cost incident to a real estate settlement,'' but does not require that each charge be calculated on a per-transaction cost basis. Section 8(c) of RESPA is evidence of the approach that regulates the underlying business relationships and procedures, in that it exempts specific kinds of business payments from being found to violate RESPA's prohibitions on kickbacks, referral fees, and unearned fees. Section 8(c)(1) establishes exemptions for payments between title companies and their agents, between lenders and their agents, and to attorneys, for services actually performed. Similar exemptions are established in subsections (c)(3) and (c)(4) for payments between real estate brokers and their agents, and among affiliated businesses. In section 8(c)(2), Congress permits settlement service providers to be compensated ''for goods or facilities actually furnished [and] for services actually performed,'' without requiring a particular, regimented pricing structure.

Section 8(c)(5) of RESPA gives the Secretary discretion to permit ''such other payments or classes of payments * * * as are specified in regulations prescribed by the Secretary, after consultation with [other Federal officials and entities].'' Through this section and section 19, the Secretary has been given broad regulatory authority to address changes in the real estate marketplace under RESPA.

HUD's current regulations implementing RESPA have sometimes been cited as obstacles to consumer-friendly business practices, however. Discussions at the RESPA Reform Roundtables during 2005 and additional comments from both industry representatives and consumer advocates have suggested the need for greater competition among settlement service providers. In light of these suggestions, the Secretary has determined that, in HUD's implementation of RESPA, there should be greater flexibility for cost pricing formulas that bring more innovation and increased price competition to the settlement process. HUD proposes to recognize in the regulations that innovative approaches such as average cost pricing and certain discounts, including volume-based discounts, may serve to lower settlement costs to consumers without violating the statutory requirements of RESPA.

The practices of negotiating price reductions—whether among settlement service providers or by an individual settlement service provider on behalf of consumers—can serve to reduce prices to consumers. Such arrangements are not contrary to the purposes of RESPA and do not violate section 8 when any and all pricing benefits are passed on to consumers. Accordingly, in today's proposed rule, HUD is amending the definition of ''thing of value'' set forth in 24 CFR 3500.14(d) to exclude discounts negotiated by settlement service providers based on negotiated pricing arrangements, provided that no more than the reduced price is charged to the borrower and disclosed on the HUD–1/1A.

In the 2002 proposed rulemaking, in the context of loan originators being subject to tolerances for their GFE estimates of settlement service charges, HUD recognized that:

> [T]he new GFE's tighter requirements on estimated third party charges may cause many loan originators not already doing so to seek to establish pricing arrangements with specific third party settlement service providers in advance, in order both to ensure they are able to meet the tolerances and to ensure lower prices for their customers. As part of negotiations for such arrangements, many originators, particularly those with a substantial volume of business, may seek prices from third party providers that are lower than those providers offer on a retail basis. However, because Section 8 of RESPA broadly prohibits providing a ''thing of value,'' which is specifically defined to include discounts, in exchange for the referral of business, many loan originators have been reluctant to openly seek such pricing benefits, even where any such discount in the price is passed on to the borrower. HUD believes that the fundamental purpose of RESPA is to lower settlement costs to borrowers, and it is therefore contrary to the law's objectives to interpret the anti-referral fee provisions of Section 8 to prohibit one settlement service provider from using its market power to negotiate discounted prices, as long as the entire discounted price negotiated by the originator is charged to the borrower and reported as part of the total charge. * * *

67 FR 49134, 49151 (July 29, 2002).

Lender comments on the 2002 Proposed Rule and discussions during the RESPA Reform Roundtables in 2005 continued to cite a need for a complete exemption from section 8 before lenders could use pricing models that would allow them to introduce more price competition in the marketplace. These comments were primarily in the context of the mortgage packaging proposal, however, and in 2002 HUD had proposed a ''safe harbor'' or section 8 exemption in that context. In advance of that proposal, HUD had determined that in order to fully develop the potential to reduce closing costs, loan originators would be able to seek discounts, including volume-based discounts, and to utilize average cost pricing. Today's proposed rule relies on adapting the GFE requirements to broaden the mortgage lending and settlement services marketplace, without a need for specific packaging proscriptions and requirements or a section 8 exemption.

HUD believes that no such exemption is necessary in order to permit average cost pricing and discounting, including volume-based discounts. Rather, HUD has determined that RESPA provides enough flexibility to permit a variety of approaches to fee calculations, so long as they do not unnecessarily increase fees charged to consumers. During the 2005 RESPA Roundtables, some loan originators and third party settlement service providers also took the position that neither a full section 8 exemption nor formal authority for packaging is needed. These providers believed that development of different pricing mechanisms and some discounts could promote market innovation and increased price competition.

In this rule, the Secretary is proposing to use the authority under section 19(a) of RESPA to permit pricing techniques using average cost pricing and certain discounts, consistent with RESPA's GFE and settlement statement requirements, and with section 8. HUD believes that consumers will ultimately benefit from negotiated pricing among and by settlement service providers. This proposed rule seeks to lower consumer costs by permitting settlement service providers who procure, or who help consumers to obtain, third party settlement services, to negotiate the pricing of those services by the third party provider. By using average cost pricing, settlement service providers could avoid having to track individual prices paid for third party services on a transaction-by-transaction basis, thereby lowering administrative costs that would be passed on to consumers.

The proposed rule would make clear that where average cost pricing is used, the evaluation of prices of third party services should focus on all of the loan originator's transactions together, rather than viewing each transaction separately. An individual borrower might be charged more or less than the actual amount paid for that service in an individual transaction, provided that borrowers are being charged no more than the average price actually received by third parties during the period in which the average price is computed.

The proposed rule sets forth two specific methods that loan originators may use to calculate an average price for a particular settlement service. The loan originator would designate a recent 6-month period as the ''averaging period'' for purposes of calculating the average price. The same average price must then be used in every transaction in that class of transactions for which a GFE is provided following the averaging period until a new averaging period is established. The average price would be calculated either as: (1) The actual average price for the settlement service during the averaging period; or (2) a projected average under a tiered pricing contract, based on the number of transactions that actually closed during the recent averaging period. If a loan originator uses one of these methods to calculate the average price for a settlement service, HUD will deem the loan originator to have complied with the requirements of the rule.

HUD welcomes comments on its proposed methods for calculating average cost prices and on any alternative methods that should be permitted. Specifically, HUD welcomes comments on how to define ''class of transactions.'' For example, ''class of transactions'' could be defined by loan type, or loan-to-value ratio. HUD is also interested in suggestions on alternative average cost pricing methods and other pricing methods that benefit consumers and are based on factors that would lead to charges to the consumer (and the disclosure of such charges) that are easily calculated, verified, and enforced, but difficult to manipulate in an abusive manner. Such factors could include, for example:

(a) Experience over a period of time that is longer or shorter than that currently provided in the proposed rule;

(b) Prices for the service among the usual third party providers upon which the lender or other settlement service usually relies;

(c) General industry practices; and

(d) A reasonable projection of future costs.

Finally, with regard to any pricing method used by a settlement service provider, if a violation of section 8 of RESPA is alleged and an investigation ensues, the proposed rule would place the burden on the targeted settlement service provider to demonstrate compliance with a permissible pricing method through the production of relevant records.

I. Changes To Strengthen Prohibition Against Requiring the Use of Affiliates

The Proposed Rule. The proposed rule would change the definition of ''required use'' in § 3500.2, so that consumers would be more likely to shop for the homes and home features, and the loans and other settlement services, that are best for them, free from the influence of disingenuous referral arrangements. HUD intends the rule to establish that, in a real estate transaction covered by RESPA, incentives that consumers may want to accept and disincentives that consumers may want to avoid should be analyzed similarly for compliance with RESPA.

This change would make it clear that HUD views economic disincentives that a consumer can avoid only by purchasing a settlement service from particular providers or businesses to which the consumer has been referred to be potentially as problematic under RESPA as are economic incentives that are contingent on the consumer's choice of a particular settlement service provider. In particular, the change proposed today may affect the analysis under section 8(a) of disincentives that are avoided only by using an affiliated settlement service provider. The change may also affect sellers who use disincentives to influence a borrower's choice of a particular title company.

Consumer business captured through economic incentive or disincentive arrangements can raise questions about violations of section 8(a) of RESPA. The change proposed today may eliminate the argument by affiliated businesses that there is no ''required use'' that prevents them from invoking the affiliated business exemption to section 8 violations that involve consumer incentives and disincentives. The modifications in the proposed rule are not intended to prevent discounts that are beneficial to consumers, however. The revised definition states that the offering by a settlement service provider of an optional package or a combination of bona fide settlement services to a borrower at a total price lower than the sum of the prices of the individual settlement services would not constitute a ''required use.'' By separate amendment to § 3500.14(d), such arrangements are defined as not being a thing of value, and so would not be in violation of the referral prohibitions in section 8(a) of RESPA.

The proposed revision to the ''required use'' definition would continue to apply in two sections of the regulations: The affiliated business exemption in § 3500.15, and the prohibition on the seller requiring the buyer to purchase title insurance from a particular company in § 3500.16. However, as part of the proposed amendment of § 3500.7, and in light of other changes that would be made by this proposed rule, the term ''required use'' would no longer apply as it does currently in § 3500.7(e).

Discussion. Section 8(a) of RESPA prohibits persons from giving or receiving a thing of value, pursuant to an agreement for the referral of business incident to a settlement service in a covered transaction. RESPA was amended in 1983 to allow businesses to make referrals to affiliated businesses, however, and to receive a benefit from their ownership interest in the affiliated businesses, so long as three conditions are met (see section 8(c)(4)).[32] One of the three conditions is that affiliated businesses may not require consumers to use any particular provider of settlement services. The term ''required use'' is currently defined in § 3500.2 of HUD's regulations to mean a situation in which a person must use a particular provider of a settlement service in order to have access to some distinct service or property. In addition, the term appears in section 9 of RESPA [33], and in §§ 3500.7(e), 3500.14(f), 3500.15(b)(2), and 3500.16 of HUD's implementing regulations.

HUD believes that some businesses have used the affiliated business arrangement exception in section 8 of RESPA to steer consumers to affiliated settlement service providers that may not provide the best mortgage products or settlement services for those consumers. A number of such complaints stem from builders, who are in a position to refer settlement service business, that use incentives or penalties to steer consumers to the builders' affiliated mortgage and title companies. Consumers have frequently contacted HUD to express concerns and register complaints about these practices, which usually fall into one of two categories.

First, consumers complain that the cost to the builders of incentives and discounts related to the homes themselves have been built into the sales price of the homes, so that they are not true incentives and discounts, but are penalties (i.e., higher sales prices) that are imposed if the consumer chooses an unaffiliated settlement service provider. Second, consumers complain that the rates and fees charged by builders' affiliated settlement service providers are higher than what would be charged by unaffiliated settlement service providers. In both of these cases, consumers may be confused about the value of the ''deal,'' and may forego shopping for lower rates and fees offered by unaffiliated settlement service providers.

For example, HUD has recently received complaints such as:

- A buyer was offered a $22,000 discount on the price of a home for using the builder's affiliated lender, but the interest rate offered by the lender was ½ point higher than the market rate, and the origination fee charged by the affiliated lender was higher.
- A buyer would be required to make a higher earnest money deposit and would lose a $2,000 ''closing incentive'' if the buyer did not use the builder's affiliated lender.
- A builder promised a $3,000 incentive on the purchase price and $6,000 toward closing costs if the buyer used the builder's affiliated lender, which charged an interest rate that was 1 percent higher than the market rate and additional fees.

The effect of the change made by the proposed rule in the definition of ''required use'' is not limited to builders and their affiliated settlement service providers. Any businesses that are either clearly affiliated because of their company structures, or that would be deemed to be in an ''affiliated business arrangement'' under RESPA's definitions of that term and the related term of ''associate,'' should be aware of the change in the definition of ''required use'' in this proposed rule. This change could affect the applicability of the affiliated business requirements to those businesses.

Further, the definition applies to all sellers of property in RESPA covered transactions, for purposes of the prohibitions in section 9 of RESPA against requiring directly or indirectly that buyers purchase title insurance from any particular title company.

HUD is requesting comments on whether the proposed change in the definition of ''required use'' will better serve the purposes of RESPA and whether further improvements could be made in the definition to accomplish the intent of both the affiliated business exemption in section 8 and the prohibition in section 9 on the required use of a title company.

J. Technical Amendments to Current RESPA Regulations

The Proposed Rule. The proposed rule would update the current RESPA regulations concerning the provision of the mortgage servicing disclosure statement within 3 days of an application for a mortgage loan, to ensure consistency with current statutory requirements. In addition, the proposed rule would update the current escrow regulations, by removing outdated provisions.

Specifically, the proposed rule would amend current § 3500.21 to conform to the Economic Growth and Regulatory Paperwork Reduction Act of 1996 (Title II of the Omnibus Consolidated Appropriations Act, 1997) (Pub. L. 104–208) (the Act). Section 2103(a) of the Act amended section 6(a) of RESPA to eliminate the requirement that applicants for federally related mortgage loans be provided a disclosure describing the lender's historical practice regarding the sale or transfer of servicing rights, and the requirement that loan applications contain signed statements from applicants acknowledging that they have read and understood the disclosure provided.

On May 9, 1997, the Department published a proposed rule (62 FR 25740) designed in part to modify HUD's existing RESPA regulations concerning the disclosure to mortgage borrowers of information pertaining to the lender's practices regarding the transfer or sale of servicing rights (RESPA section 6(a)), in order to make the regulations consistent with 1996 statutory amendments effected by the Economic Growth and Regulatory Paperwork Reduction Act. The Department received numerous comments on the proposed rule, and the comments were generally favorable. However, the Department never finalized that proposed rule. Due to the amount of time that has passed since the first proposed rule, today's proposed rule seeks comment on changes to conform the transfer of servicing disclosure requirements to the current statutory requirements.

In addition, the proposed rule would make changes to current § 3500.17 to eliminate the phase-in period for aggregate accounting for escrow accounts. The phase-in period was a transitional provision that expired on October 27, 1997. All servicers are currently required to use the aggregate accounting method. Today's proposed

[32] Section 8(c)(4) (12 U.S.C. 2607(c)(4)) of RESPA states in part that ''Nothing in this section shall be construed as prohibiting * * * affiliated business arrangements so long as (A) a disclosure is made of the existence of such an arrangement to the person being referred * * *, (B) such person is not required to use any particular provider of settlement services, and (C) the only thing of value that is received from the arrangement, other than the payments permitted under this subsection, is a return on the ownership interest * * *.''

[33] Section 9 states in part that ''[n]o seller of property * * * shall require directly or indirectly, as a condition to selling the property, that title insurance covering the property be purchased by the buyer from any particular title company.''

rule would clarify this by eliminating provisions from § 3500.17 that relate only to the alternate accounting methods that were permitted during the phase-in period.

K. ESIGN Applicability to RESPA Disclosures

The Proposed Rule. The proposed rule would amend HUD's RESPA rules to explicitly recognize the current statutory applicability of the Electronic Signatures in Global and National Commerce Act (ESIGN), 15 U.S.C. 7001–7031, to RESPA. This amendment is intended to make clear that all RESPA disclosures may be provided to consumers in electronic form, so long as the consumer consents to receive such disclosures in electronic form and the other specific conditions of ESIGN are met. This recognition of the applicability of ESIGN to RESPA would also make clear that all documents required to be retained under RESPA may be retained in electronic format, so long as the ESIGN requirements for document retention are met.

V. Questions for Commenters

HUD welcomes comments on all aspects of the proposal. In addition, HUD specifically requests comment on the following issues:

1. Whether a 12-month implementation period for the GFE is appropriate. (Section IV.D.)
2. The proposed GFE, as well as the proposed HUD–1/1A Settlement Statement Forms.
3. Possible additional ways to increase consumer understanding of adjustable rate mortgages.
4. Whether the proposed requirements for completing and delivering the Addendum to the HUD–1/1A, including the mandatory reading of the Closing Script by the party conducting the closing to the borrower(s), are the best methods for assuring that borrower(s) understand their loan terms and the differences between the GFE and the HUD–1/1A.
5. Whether a provision should be added to the RESPA regulations allowing a loan originator, for a limited time after closing, to address the failure to comply with tolerances under the proposed GFE requirements, and if so, how should such a provision be structured? (Section IV.E. 10) Would such a provision be useful, and if so, what would be the appropriate time frame for finding and refunding excess charges? Could such a provision be abused, and therefore harmful to consumers? Would the ability of prosecutors to exercise enforcement discretion obviate the need for such a provision?
6. Proposed methods for calculating average cost prices and on any alternative methods that should be permitted. (Section IV.H.) Specifically, how to define ''class of transactions.'' Comments are also invited on alternative average cost pricing methods and other pricing methods that benefit consumers and are based on factors that would lead to charges to the consumer and disclosure of such charges that are easily calculated, verified, and enforced, but difficult to manipulate in an abusive manner. Such factors could include:
(a) Experience over a period of time that is longer or shorter than that currently provided in the proposed rule;
(b) Prices for the service among the usual third party providers upon which the lender or other settlement service usually relies;
(c) General industry practices; and
(d) A reasonable projection of future costs.
7. Whether the proposed change in the definition of ''required use'' will better serve the purposes of RESPA and whether further improvements could be made in the definition to accomplish the intent of both the affiliated business exemption in section 8 and the prohibition in section 9 on the required use of a title company. (Section IV.I.)
8. With respect to the revised definition of ''Good Faith Estimate'' set forth in the proposed rule language at 24 CFR 3500.2, is the standard set forth sufficient to ensure that good faith estimates will be filled out consistently by all loan originators in a particular community?
9. Should the Section 6 disclosure on transfer of servicing that is required under RESPA be included on the GFE?
10. Should a loan originator be required to include a ''no cost loan'' on the trade-off chart on page 3 of the GFE as one of the alternative loans if it is not the loan for which the GFE is written?

VI. Findings and Certifications

The Paperwork Reduction Act

Information Collection Requirements

The information collection requirements contained in this proposed rule have been submitted to the Office of Management and Budget (OMB) under the Paperwork Reduction Act of 1995 (44 U.S.C. 3501–3520). In accordance with the Paperwork Reduction Act, an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information, unless the collection displays a currently valid OMB control number.

The burden of the information collections in this proposed rule is estimated as follows:

REPORTING AND RECORDKEEPING BURDEN

Information collection	Number of respondents	Frequency of response	Responses per annum	Burden hour per response	Annual burden hours	Hourly cost	Annual cost
GFE/Information Booklet	50,000	425	21,250,000	0.17	5,3,612,500	$31.14	$112,493,250
Servicing Disclosure	0	0	0	0	0	0	0
Transfer Disclosure	20,000	3,000	60,000,000	0.03	1,800,000	10.00	18,000,000
HUD–1 or HUD–1A and Closing Script	20,000	625	12,500,000	0.58	7,250,000	33.74	244,615,000
Initial Escrow	2,000	4,875	9,750,000	0.08	780,000	* 0.00	0
Annual Escrow	2,000	21,100	42,200,000	0.08	3,376,000	* 20.00	67,520,000
Voluntary Escrow Account Payments	2,000	600	1,200,000	0.08	99,600	20.00	1,920,000
AfBA	10,000	269	2,689,500	0.10	268,950	20.00	5,379,000
Totals			149,589,500		17,183,450		$449,927,250

In accordance with 5 CFR 1320.8(d)(1), HUD is soliciting comments from members of the public and affected agencies concerning this collection of information to:

(1) Evaluate whether the proposed collection of information is necessary for the proper performance of the functions of the agency, including whether the information will have practical utility;

(2) Evaluate the accuracy of the agency's estimate of the burden of the proposed collection of information;

(3) Enhance the quality, utility, and clarity of the information to be collected; and

(4) Minimize the burden of the collection of information on those who are to respond; including through the use of appropriate automated collection techniques or other forms of information technology, e.g., permitting electronic submission of responses.

Interested persons are invited to submit comments regarding the information collection requirements in this rule. Under the provisions of 5 CFR part 1320, OMB is required to make a decision concerning this collection of information between 30 and 60 days after today's publication date. Therefore, a comment on the information collection requirements is best assured of having its full effect if OMB receives the comment within 30 days of today's publication. Comments must refer to the proposal by name and docket number (FR–5180) and must be sent to: HUD Desk Officer, Office of Management and Budget, New Executive Office Building, Washington, DC 20503, Fax number: (202) 395–6947 and Reports Liaison Officer, Office of Housing—Federal Housing Commissioner, Department of Housing and Urban Development, 451 Seventh Street, SW., Room 9136, Washington, DC 20410–8000.

Environmental Impact

A Finding of No Significant Impact with respect to the environment has been made in accordance with HUD regulations at 24 CFR part 50, which implement section 102(2)(C) of the National Environmental Policy Act of 1969 (42 U.S.C. 4332(2)(C)). The Finding of No Significant Impact is available for public inspection between the hours of 8 a.m. and 5 p.m. weekdays in the Regulations Division, Office of General Counsel, U.S. Department of Housing and Urban Development, 451 Seventh Street, SW., Room 10276, Washington, DC 20410–0500. Due to security measures at the HUD Headquarters building, an advance appointment to review the public comments must be scheduled by calling the Regulations Division at (202) 402–3055 (this is not a toll-free number). Individuals with speech or hearing impairments may access this number via TTY by calling the toll-free Federal Information Relay Service at (800) 877–8339.

Executive Order 12866, Regulatory Planning and Review

OMB reviewed this proposed rule under Executive Order 12866 (entitled ''Regulatory Planning and Review''), which the President issued on September 30, 1993. This rule was determined economically significant under the executive order. Any changes made to the proposed rule subsequent to its submission to OMB are identified in the docket file, which is available for public inspection in the Regulations Division, Office of General Counsel, U.S. Department of Housing and Urban Development, 451 Seventh Street, SW., Room 10276, Washington, DC 20410–0500. The Initial Economic Analysis prepared for this rule is available online at *http://www.hud.gov/respa*, and for public inspection in the Regulations Division. Due to security measures at the HUD Headquarters building, an advance appointment to review the public comments must be scheduled by calling the Regulations Division at (202) 402–3055 (this is not a toll-free number). Individuals with speech or hearing impairments may access this number through TTY by calling the Federal Information Relay Service at (800) 877–8339.

Federalism Impact

This proposed rule does not have federalism implications and does not impose substantial direct compliance costs on state and local governments or preempt state law within the meaning of Executive Order 13132 (entitled ''Federalism'').

Regulatory Flexibility Act

The Secretary, in accordance with the Regulatory Flexibility Act (5 U.S.C. 605(b)), has reviewed and approved this proposed rule and has determined that the rule would have a significant economic impact on a substantial number of small entities within the meaning of the Regulatory Flexibility Act.

In accordance with section 603 of the Regulatory Flexibility Act, an Initial Regulatory Flexibility Analysis (IRFA) has been prepared and has been made part of the Economic Analysis prepared under Executive Order 12866. The IRFA portion, however, of the combined analysis is published as an appendix to this proposed rule. The IRFA was also submitted to the Chief Counsel for Advocacy of the Small Business Administration for review and comment on its impact on business.

Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (2 U.S.C. 1531–1538) (UMRA) requires federal agencies to assess the effects of their regulatory actions on state, local, and tribal governments and on the private sector. This proposed rule does not, within the meaning of the UMRA, impose any federal mandates on any state, local, or tribal governments nor on the private sector.

Congressional Review of Final Rules

This rule constitutes a ''major rule'' as defined in the Congressional Review Act (5 U.S.C. Chapter 8). At the final rule stage, this rule will have a 60-day delayed effective date and be submitted to the Congress in accordance with the requirements of the Congressional Review Act.

List of Subjects

24 CFR Part 203

Hawaiian Natives, Home improvement, Indians—lands, Loan programs—housing and community development, Mortgage insurance, Reporting and recordkeeping requirements, Solar energy.

24 CFR Part 3500

Consumer protection, Condominiums, Housing, Mortgagees, Mortgage servicing, Reporting, and Recordkeeping requirements.

For the reasons stated in the preamble, HUD proposes to amend 24 CFR parts 203 and 3500 as follows:

PART 203 — SINGLE FAMILY MORTGAGE INSURANCE

1. The authority citation for part 203 continues to read as follows:

Authority: 12 U.S.C. 1709, 1710, 1715b, 1715z–16, and 1715u; 42 U.S.C. 3535(d).

2. In § 203.27, paragraph (a)(2) is revised to read as follows:

§ 203.27 Charges, fees, or discounts.

(a) * * *

(2) A charge to compensate the mortgagee for expenses incurred in originating and closing the loan, *provided* that the Commissioner may establish limitations on the amount of any such charge.

* * * * *

PART 3500—REAL ESTATE SETTLEMENT PROCEDURES ACT

3. The authority citation for part 3500 continues to read as follows:

Authority: 12 U.S.C. 2601 *et seq.*; 42 U.S.C. 3535(d).

4. In § 3500.2, paragraph (b) is amended by removing the definition of Application; revising the definitions of *Good faith estimate or GFE, Mortgage broker*; and *Required use* and add, in alphabetical order, the following new definitions of *Adjustable rate, Balloon payment, Closing script, Credit or charge for the specific interest rate chosen, Good faith estimate applicant or GFE applicant, Good faith estimate application or GFE application, Loan originator, Mortgage application, Origination service, Prepayment penalty, Primary title service, Third party, Tolerance, and Unforeseeable circumstances* to read as follows:

§ 3500.2 Definitions.

* * * * *

(b) * * *

Adjustable rate has the same meaning as ''adjustable rate'' under the Truth in Lending Act, 15 U.S.C. 1601 *et seq.* (''TILA'').

Balloon payment has the same meaning as ''balloon payment'' under the Truth in Lending Act, 15 U.S.C. 1601 *et seq.* (''TILA'').

* * * * *

Closing script means the disclosure document prepared for the closing by the settlement agent, pursuant to information provided by the loan originator, that compares the loan terms and settlement charges estimated on the GFE with the HUD–1/HUD–1A and that describes, in detail, the required loan terms for the specific mortgage loan and related settlement information. It is an addendum to the HUD–1/HUD–1A.

Credit or charge for the specific interest rate chosen means, for a mortgage broker, the credit or charge for the specific interest rate chosen is the difference between the initial loan amount and the payment to the mortgage broker (i.e., the sum of the price paid for the loan by the lender and any other payments to the mortgage broker from the lender). When the amount paid to the mortgage broker exceeds the initial loan amount, there is a credit to the borrower and it is entered as a negative amount in block 2 of the GFE. When the initial loan amount exceeds the amount paid to the mortgage broker, there is a charge to the borrower and it is entered as a positive amount in block 2 of the GFE.

* * * * *

Good faith estimate or *GFE* means an estimate of settlement charges a borrower is likely to incur, as a dollar amount, and related loan information, based upon common practice and experience in the locality of the mortgaged property, provided on the form prescribed in Appendix C to this part that is prepared in accordance with § 3500.7 and the Instructions in Appendix C to this part.

Good faith estimate applicant or *GFE applicant* means any prospective borrower for a federally related mortgage loan who submits a GFE application.

Good faith estimate application or *GFE application* means a written or oral submission to a loan originator by a prospective borrower to obtain a GFE for a specific loan product. The loan originator may require the GFE applicant to provide no more than the prospective borrower's name, Social Security number, property address, monthly income, the borrower's best estimate of the value of the property, and the mortgage loan amount sought by the borrower to obtain a GFE. A GFE application shall either be in writing or electronically submitted, including a written record of an oral application, so that the loan originator can retain a record of the application. If the submission does not state or identify a specific property, the submission is not a GFE application. The subsequent addition of an identified property to the submission converts the submission to a GFE application. Neither a GFE application nor an application for a prequalification is a mortgage application for a federally related mortgage under this part.

* * * * *

Loan originator means a lender or mortgage broker.

* * * * *

Mortgage application means a submission to a loan originator by a prospective borrower of such financial and other information, whether written or computer-generated, as a loan originator may require to begin final underwriting, and such other steps as are necessary to originate a mortgage loan for the prospective borrower.

Mortgage broker means a person (not an employee of a lender) or entity that renders origination services in a table funded or intermediary transaction. A loan correspondent approved under 24 CFR 202.8 for Federal Housing Administration programs is a mortgage broker for purposes of this part.

* * * * *

Origination service means any service involved in the creation of a mortgage loan, including but not limited to the taking of loan applications, loan processing, and the underwriting and funding of loans, and the processing and administrative services required to perform these functions.

* * * * *

Prepayment penalty has the same meaning as ''prepayment penalty'' under the Truth in Lending Act, 15 U.S.C. 1601 *et seq.* (''TILA'').

Primary title service means any service involved in the provision of title insurance (lender or owner policy) and settlement or closing services, including but not limited to: title examination and evaluation; preparation and issuance of title commitment; clearance of underwriting objections; preparation and issuance of a title insurance policy or policies; and the processing and administrative services required to perform these functions.

* * * * *

Required use means a situation in which a borrower's access to some distinct service, property, discount, rebate, or other economic incentive, or the borrower's ability to avoid an economic disincentive or penalty, is contingent upon the borrower using or failing to use a referred provider of settlement services. However, the offering by a settlement service provider of an optional combination of *bona fide* settlement services to a borrower at a total price lower than the sum of the prices of the individual settlement services does not constitute a required use.

* * * * *

Third party means a settlement service provider other than a loan originator.

* * * * *

Tolerance means the maximum amount by which the charge for a category or categories of settlement costs may exceed the amount of the estimate for such category or categories on a GFE.

Unforeseeable circumstances means:

(1) Acts of God, war, disaster, or other emergency making it impossible or impracticable for the loan originator to complete the transaction; and

(2) Circumstances that could not be reasonably foreseen by a loan originator at the time of GFE application that are particular to the transaction and that result in increased costs, such as a change in the property purchase price, boundary disputes, the need for a second appraisal or flood insurance, or environmental problems. Market fluctuations by themselves shall not be considered unforeseeable circumstances.

§ 3500.6 [Amended]

5. Section 3500.6 is amended in paragraph (a) introductory text by adding ''GFE or a'' before ''federally related mortgage loan'', and in paragraph (a)(1) by adding ''GFE'' before the word ''application'' the first time it appears.

6. In § 3500.7, the section heading and paragraphs (a) through (e) are revised; paragraph (f) is redesignated as paragraph (g); and new paragraphs (f) and (h) are added, as follows:

§ 3500.7 Good faith estimate or GFE.

(a) *Lender to provide.* (1) Except as otherwise provided in paragraphs (a), (b), or (g) of this section, not later than 3 business days after a lender receives a GFE application from a GFE applicant, or information sufficient to complete a GFE application, the lender must provide the GFE applicant with a GFE. In the case of dealer loans, the lender must either provide the GFE or ensure that the dealer provides the GFE.

(2) The lender must provide the GFE to the GFE applicant by hand delivery, by placing it in the mail, or, if the GFE applicant agrees, by fax, email, or other electronic means.

(3) The lender is not required to provide the GFE applicant with a GFE if, before the end of the 3-business-day period:

(i) The lender denies the GFE application of the GFE applicant;

(ii) The lender denies the mortgage application of the GFE applicant; or

(iii) The applicant withdraws its GFE application.

(4) The lender is not permitted to collect, as a condition for providing a GFE, any fee for an appraisal, inspection, or other similar service needed for final underwriting. The lender may, at its option, collect a fee limited to the cost of providing the GFE, including the cost of an initial credit report.

(b) *Mortgage broker to provide.* (1) Except as otherwise provided in paragraphs (b) or (g) of this section, either the lender or the mortgage broker must provide a GFE to the GFE applicant not later than 3 business days after a mortgage broker receives from the GFE applicant either a GFE application or information sufficient to complete a GFE application. The lender is responsible for ascertaining whether the GFE has been provided. If the mortgage broker has provided a GFE that is acceptable to the lender, the lender is not required to provide an additional GFE.

(2) The mortgage broker must provide the GFE by hand delivery, by mail, or, if the applicant agrees, by fax, email, or other electronic means.

(3) The mortgage broker is not required to provide the GFE applicant with a GFE if, before the end of the 3-business-day period:

(i) The mortgage broker or lender denies the GFE application of the GFE applicant;

(ii) The mortgage broker or lender denies the mortgage application of the GFE applicant; or

(iii) The applicant withdraws its GFE application.

(4) The mortgage broker is not permitted to collect, as a condition for providing a GFE, any fee for an appraisal, inspection, or other similar service needed for final underwriting. The mortgage broker may, at its option, collect a fee limited to the cost of providing the GFE, including the cost of an initial credit report.

(c) *Availability of GFE terms.* The estimate of the charges for all settlement services other than the charge or credit for the interest rate chosen, the adjusted origination charges, and per diem interest must be available until 10 business days from when the GFE is delivered, but it may remain available longer, if the loan originator extends the period of availability. Once a mortgage application is submitted to the loan originator, the non-interest rate-dependent settlement charges of the GFE that is the basis for the mortgage application must remain in effect until closing. If the interest rate was not locked when the mortgage application was submitted, or a locked interest rate has expired, all interest rate-dependent charges and disclosures may change. If the GFE applicant notifies the loan originator to proceed with a mortgage application after the period of availability has expired, the loan originator may:

(1) Continue to abide by the terms and conditions contained within the GFE for which the period of availability has expired;

(2) Deny the GFE applicant an opportunity to submit a mortgage application at that time for that specific loan because the applicant did not respond within the period of availability; or

(3) Provide a new GFE for a new loan to the GFE applicant within 3 business days.

(d) *Content and form of GFE.* The loan originator must prepare the GFE in accordance with the requirements of this section and the Instructions in Appendix C to this part when preparing the GFE Form in Appendix C to this part. The instructions in Appendix C to this part allow for flexibility in the preparation and distribution of the GFE in hard copy and electronic format.

(e) *Tolerances for amounts included on GFE.* (1) Absent unforeseeable circumstances, the actual charges at settlement may not exceed the amounts included on the GFE for:

(i) The loan originator's service charge;

(ii) While the borrower's interest rate is locked, the credit or charge for the interest rate chosen;

(iii) While the borrower's interest rate is locked, the adjusted origination charge; and

(iv) Government recording and transfer charges.

(2) Absent unforeseeable circumstances, the sum of the charges at settlement for the following services may not be greater than 10 percent above the sum of the amounts included on the GFE:

(i) Lender-required settlement services, where the lender selects the third party settlement service provider; and

(ii) Lender-required services, and optional owner's title insurance selected by the borrower, when the borrower uses a settlement service provider identified by the loan originator.

(3) The amounts charged for all other settlement services included on the GFE may change at settlement.

(4) If a loan originator cannot meet the tolerances under this section because of unforeseeable circumstances, the loan originator must document the unforeseeable circumstances that resulted in the increased costs and charge the borrower only the amount of the increased costs. In such situations, the loan originator must notify the borrower within 3 business days of the increase in charges arising from the unforeseeable circumstances, and a new GFE reflecting the revised charges must be provided to the borrower.

(5) Loan originators must retain documentation of any unforeseeable circumstances resulting in final costs in excess of the established tolerances for amounts stated on GFEs for no less than 3 years after settlement.

(f) *Changes to the GFE.* (1) The loan originator must complete final underwriting within a reasonable time after a borrower's mortgage application is complete. If final underwriting or unforeseeable circumstances result in a change in the borrower's eligibility for the specific loan terms identified in the GFE, the loan originator must:

(i) Notify the borrower within one business day of the decision to reject the loan;

(ii) If another loan is made available, provide a revised GFE to the borrower; and

(iii) Document the reasons for the revised GFE and retain the documentation for no less than 3 years after settlement.

(2) If a borrower requests changes to the mortgage loan identified in the GFE that change the settlement charges or the terms of the loan, the loan originator is no longer bound by the GFE, and the loan originator must:

(i) Notify the borrower within one business day of the decision to reject the loan;

(ii) If another loan is made available, provide a revised GFE to the borrower; and

(iii) Document the reasons for the revised GFE and retain the documentation for no less than 3 years after settlement.

(3) In transactions involving new home purchases, where settlement is anticipated to occur more than 60 days from the time of a GFE application, the loan originator may provide the GFE to the borrower with a clear and conspicuous disclosure stating that at any time up until 60 days prior to closing, the loan originator may issue a revised GFE. If no such separate disclosure is provided, the loan originator cannot issue a revised GFE, except as otherwise provided in paragraph (f) of this section.

* * * * *

(h) *Violations of section 5 of RESPA (12 U.S.C. 2604).* A loan originator that violates the requirements of this section, including by exceeding the charges listed on the GFE at settlement by more than the permitted tolerances, shall be deemed to have violated section 5 of RESPA.

7. In § 3500.8, paragraphs (b) and (c) are revised; and new paragraphs (d) and (e) are added to read as follows:

§ 3500.8 Use of HUD–1 or HUD–1A settlement statements.

* * * * *

(b) *Charges to be stated.* The settlement agent shall complete the HUD–1 or HUD–1A in accordance with the instructions set forth in Appendix A to this part.

(1) *In general.* The settlement agent shall state the actual charges paid by the borrower and seller on the HUD–1 or HUD–1A. The settlement agent must separately itemize each third party charge paid by the borrower and seller. Origination services performed by or on behalf of the loan originator must be included in the loan originator's own charge. Primary title services performed by or on behalf of the title underwriter or title agent must be included in the title underwriter's or title agent's own charge. The amount stated on the HUD–1 or HUD–1A for any itemized service cannot exceed the amount actually received by the third party for that itemized service, unless the charge is based on an average cost price in accordance with paragraph (b)(2) of this section.

(2) *Average cost pricing.* (i) The charge shown on the HUD–1 or HUD–1A for a settlement service provided by a third party may be an average price calculated based on either of the following methods:

(A) The average price used on a HUD–1 or HUD–1A may be based on the actual average price for that service in all loans closed by the loan originator, on a national or more limited basis, during the averaging period; or

(B) The average price used on a HUD–1 or HUD–1A may be based on a tiered pricing contract, provided the projected number of loans used in calculating the average is equal to the number of loans actually closed by the loan originator during the averaging period.

(ii) For purposes of calculating an average price, the averaging period must be a specific recent period of 6 consecutive months preceding the receipt of a GFE application, as designated by the loan originator. The same method of determining the averaging period must be used for each borrower from whom a GFE application is received, until such time as the average is recomputed.

(iii) If a loan originator uses average cost pricing for any class of transactions in a particular period, the loan originator must use the same average cost price in every transaction within that class for which a borrower's GFE application was received during that period.

(iv) The loan originator must retain all documentation that the average cost pricing is accurate in a given time period, under the pricing formula used, for at least 3 years.

(c) *Aggregate accounting at settlement.* After itemizing individual deposits in the 1000 series, the servicer must make an adjustment based on aggregate accounting. This adjustment equals the difference in the deposit required under aggregate accounting and the sum of the itemized deposits. The computation steps for aggregate accounting are set out in § 3500.17(d). The adjustment will always be a negative number or zero (-0-). The settlement agent shall enter the aggregate adjustment amount on a final line in the 1000 series of the HUD–1 or HUD–1A statement. Appendix E to this part sets out an example of aggregate analysis. Appendix A to this part contains instructions for completing the HUD–1 or HUD–1A settlement statements using an aggregate analysis adjustment.

(d) *Closing script.* (1) The loan originator must transmit to the settlement agent all information necessary to complete the prescribed closing script disclosure document, which is an addendum to the HUD–1/1A settlement form and is prepared by the settlement agent. This addendum must accurately reflect the required information provided by the loan originator regarding the loan terms and related settlement information.

(2) The settlement agent or other person conducting the closing must read the closing script aloud to the borrower and explain:

(i) The comparison between the final settlement charges listed on the HUD–1/1A settlement form and the estimate of charges listed on the GFE;

(ii) Whether or not the tolerances have been met; and

(iii) Other required loan information as shown on the closing script addendum forms in Appendix A to this part.

(3) Any inconsistencies between the loan documents (including the mortgage note) and the summary of loan terms on the GFE, and between the HUD–1/1A settlement charges and the charges stated on the GFE, must be disclosed and explained to the borrower.

(4) Upon request of the borrower, the HUD–1/1A and the closing script addendum must be made available for review by the borrower 24 hours prior to the closing in accordance with § 3500.10(a). The closing script addendum must be delivered to the borrower with the HUD–1/1A at the closing in accordance with § 3500.10(a) and (c). The prescribed closing script addendum formats, with instructions, are set forth in Appendix A to this part.

(e) *Violations of section 4 of RESPA (12 U.S.C. 2604).* A violation of any of the requirements of this section will be deemed to be a violation of section 4 of RESPA.

§ 3500.10 [Amended].

8. Section 3500.10 is amended by adding the phrase '', with addendum,'' as follows:

a. In paragraph (a) after the word ''statement'';

b. In paragraph (b) after the reference ''HUD–1A'' in the first and last sentences; and

c. In paragraphs (c), (d), and (e) after each reference to ''HUD–1A''.

9. In § 3500.14, the text after the heading in paragraph (d) is redesignated

as paragraph (d)(1), and new paragraph (d)(2) is added, to read as follows:

§ 3500.14 Prohibition against kickbacks and unearned fees.

* * * * *

(d) Thing of value. (1) * * *

(2) A discount negotiated by settlement service providers in the price of a third party settlement service is not a thing of value, provided that no more than the discounted price is charged to the borrower and disclosed on the HUD–1/1A.

* * * * *

10. Section 3500.17 is amended:

a. In paragraph (b) by removing the definitions of *Acceptable accounting method, Conversion date, Phase-in period, Post-rule account,* and *Pre-rule account;*

b. In paragraph (c) by revising the heading and paragraphs (c)(4), (5), (6), and (8);

c. In paragraph (d) by removing paragraph (d)(2), redesignating paragraph (d)(1) as paragraph (d)(2), revising newly designated paragraph (d)(2)(i) introductory text, and redesignating the introductory text as paragraph (d)(1) and revising it; and

d. In paragraph (e) by removing paragraph (e)(3), to read as follows:

§ 3500.17 Escrow accounts.

* * * * *

(c) *Limits on payments to escrow accounts.* * * *

(4) *Aggregate accounting required.* All servicers must use the aggregate accounting method in conducting escrow account analyses.

(5) *Cushion.* The cushion must be no greater than one-sixth (1/6) of the estimated total annual disbursements from the escrow account.

(6) *Restrictions on pre-accrual.* A servicer must not practice pre-accrual.

* * * * *

(8) *Provisions in mortgage documents.* The servicer must examine the mortgage loan documents to determine the applicable cushion for each escrow account. If the mortgage loan documents provide for lower cushion limits, then the terms of the loan documents apply. Where the terms of any mortgage loan document allow greater payments to an escrow account than allowed by this section, then this section controls the applicable limits. Where the mortgage loan documents do not specifically establish an escrow account, whether a servicer may establish an escrow account for the loan is a matter for determination by State law. If the mortgage loan document is silent on the escrow account limits and a servicer establishes an escrow account under State law, then the limitations of this section apply unless State law provides for a lower amount. If the loan documents provide for escrow accounts up to the RESPA limits, then the servicer may require the maximum amounts consistent with this section, unless an applicable State law sets a lesser amount.

* * * * *

(d) *Methods of escrow account analysis.* (1) The following sets forth the steps servicers must use to determine whether their use of aggregate analysis conforms with the limitations in § 3500.17(c)(1). The steps set forth in this section result in maximum limits. Servicers may use accounting procedures that result in lower target balances. In particular, servicers may use a cushion less than the permissible cushion or no cushion at all. This section does not require the use of a cushion.

(2) *Aggregate analysis.* (i) In conducting the escrow account analysis using aggregate analysis, the target balances may not exceed the balances computed according to the following arithmetic operations:

* * * * *

11. Section 3500.21 is amended by revising paragraphs (b) and (c) to read as follows:

§ 3500.21 Mortgage servicing transfers.

* * * * *

(b) *Servicing Disclosure Statement; Requirements.* (1) At the time a GFE application for a mortgage servicing loan is submitted, or within 3 business days after submission of the GFE application, the lender, mortgage broker who anticipates using table funding, or dealer who anticipates a first lien dealer loan shall provide to each person who applies for such a loan a Servicing Disclosure Statement. A format for the Servicing Disclosure Statement appears as Appendix MS–1 to this part. The specific language of the Servicing Disclosure Statement is not required to be used. The information set forth in ''Instructions to Preparer'' on the Servicing Disclosure Statement need not be included with the information given to applicants, and material in square brackets is optional or alternative language. The model format may be annotated with additional information that clarifies or enhances the model language. The lender, table funding mortgage broker, or dealer should use the language that best describes the particular circumstances.

(2) The Servicing Disclosure Statement must indicate whether the servicing of the loan may be assigned, sold, or transferred to any other person at any time while the loan is outstanding. If the lender, table funding mortgage broker, or dealer in a first lien dealer loan will not engage in the servicing of the mortgage loan for which the applicant has applied, the disclosure may consist of a statement that such entity intends to assign, sell, or transfer servicing of such mortgage loan before the first payment is due. Alternatively, if the lender, table funding mortgage broker, or dealer in a first lien dealer loan will engage in the servicing of the mortgage loan for which the applicant has applied, the disclosure may consist of a statement that the entity will service such loan and does not intend to sell, transfer, or assign the servicing of the loan.

(c) *Servicing Disclosure Statement; Delivery.* The lender, table funding mortgage broker, or dealer that anticipates a first lien dealer loan shall deliver Servicing Disclosure Statements to each applicant for a mortgage servicing loan at the time a GFE application is received, or by placing it in the mail with prepaid first-class postage within 3 business days from receipt of the GFE application. In the event the borrower is denied credit within the 3 business-day period, no servicing disclosure statement is required to be delivered. If co-applicants indicate the same address on their GFE application, one copy delivered to that address is sufficient. If different addresses are shown by co-applicants on the GFE application, a copy must be delivered to each of the co-applicants.

* * * * *

12. A new § 3500.22 is added to read as follows:

§ 3500.22 Severability.

If any particular provision of this part or the application of any particular provision to any person or circumstance is held invalid, the remainder of this part and the application of such provisions to other persons or circumstances shall not be affected by such holding.

13. A new § 3500.23 is added to read as follows:

§ 3500.23 ESIGN applicability.

The Electronic Signatures in Global and National Commerce Act (''ESIGN''), 15 U.S.C. 7001–7031, shall apply to this part.

14. Appendix A to part 3500 is amended:

a. By revising the first two sentences of the first paragraph of the Appendix;

b. By removing the second paragraph of the General Instructions and adding four new paragraphs in its place;

c. By revising the first paragraph after the heading ''Section L. Settlement Charges'';

d. By revising the paragraphs for ''Line 801'' through ''Lines 808–811'' after the heading ''Section L. Settlement Charges'';

e. By revising the second paragraph and removing the third paragraph of instructions for ''Lines 1000–1008'' after the heading ''Section L. Settlement Charges'', and by removing the heading for the instructions for ''Lines 1000–1008'' and adding in its place ''Lines 1000–1009'';

f. By removing the paragraphs for ''Lines 1100–1113'' through ''Lines 1111–1113'' after the heading ''Section L. Settlement Charges'' and adding in their place nine paragraphs of instructions for lines 1100–1114;

g. By removing the paragraph for ''Lines 1201–1205'' after the heading ''Section L. Settlement Charges'' and adding in its place two paragraphs of instructions for lines 1200–1205;

h. By removing the paragraphs for ''Lines 1301 and 1302'' and for ''Lines 1303–1305'' after the heading ''Section L. Settlement Charges'' and adding in their place a paragraph of instructions for lines 1301–1305;

i. By revising the paragraph for ''Line 1400'';

j. By revising the first sentence in the first paragraph following the heading ''Line Item Instructions for Completing HUD–1A'';

k. By adding after the paragraph of instructions for ''Line 1604'' a new heading ''General Instructions for Completing Closing Script Addendum to HUD–1/1A Settlement Form'' and a new paragraph of instructions;

l. By revising the Forms ''Settlement Statement'' and ''Settlement Statement Optional Form for Transactions without Sellers''; and

m. By adding new Instructions to Closing Script Preparer and Examples of Completed Closing Scripts 1 through 6, as follows:

APPENDIX A TO PART 3500—INSTRUCTIONS FOR COMPLETING HUD–1 AND HUD–1A SETTLEMENT STATEMENTS; SAMPLE HUD–1 AND HUD–1A STATEMENTS

The following are instructions for completing sections A through L and the closing script addendum of the HUD–1 settlement statement, required under section 4 of RESPA and Regulation X of the Department of Housing and Urban Development (24 CFR part 3500). This form is to be used as a statement of actual charges and adjustments paid by the borrower and the seller and received by each settlement service provider, to be given to the parties in connection with the settlement. * * *

General Instructions

* * * * *

The settlement agent shall complete the HUD–1 to itemize all charges imposed upon the Borrower and the Seller by the loan originator and all sales commissions, whether to be paid at settlement or outside of settlement, and any other charges which either the Borrower or the Seller will pay at settlement. For all items except for those paid to and retained by the loan originator, the name of the person or firm ultimately receiving the payment must be shown together with the total amount paid to such person in connection with the transaction. Charges that are customarily paid for by the seller must be shown in the seller's column on page 2 of the HUD–1 (unless paid outside closing), and charges that are customarily paid for by the borrower must be shown in the borrower's column (unless paid outside closing). If a seller pays for a charge that is customarily paid for by the borrower, the charge should not be shown on page 2 of the HUD–1 but instead should be listed as an adjustment in lines 506–509 of the HUD–1. If a borrower pays for a charge that is customarily paid for by the seller, the charge should not be shown on page 2 of the HUD–1, but instead should be listed as an adjustment in lines 204–209 of the HUD–1.

Charges to be paid outside of settlement by the borrower, seller, or loan originator, including cases where a non-settlement agent (i.e., attorneys, title companies, escrow agents, real estate agents, or brokers) holds the Borrower's deposit toward the sales price (earnest money) and applies the entire deposit towards the charge for the settlement service it is rendering, must be included on the HUD–1 but marked ''P.O.C.'' for ''Paid Outside of Closing'' (settlement) and cannot be included in computing totals. P.O.C. items must not be placed in the Borrower or Seller columns, but rather on the appropriate line next to the columns. The settlement agent must indicate whether P.O.C. items are paid for by the Borrower, Seller, or some other party by marking the items paid for by whoever made the payment as ''P.O.C. (payor).''

In the case of ''no cost'' loans where ''no cost'' encompasses third party fees as well as the up-front payment to the loan originator, the third party services to be paid for out of the adjusted origination charge must be itemized and listed on the HUD–1/1A with the charge for the third party service. These itemized charges must be recorded in the columns.

For charges disclosed using average cost pricing, the amount stated on the HUD–1 Settlement Statement as a charge to the borrower or seller for the settlement service must be the average price established pursuant to 24 CFR 3500.8(e).

* * * * *

Line Item Instructions

Section L. Settlement Charges

For all items except for those paid to and retained by the loan originator, the name of the person or firm ultimately receiving the payment must be shown. In the case of loans where third party settlement services, other than origination services, are paid from the adjusted origination charge by the loan originator, the individual third party settlement services should be itemized, with the charges shown in the columns. In those cases, the adjusted origination charge in line 803 will be a negative number large enough to offset the amounts of the third party settlement services that are paid out of the adjusted origination charge.

* * * * *

Line 801 is used to record ''Our Service Charge,'' which is received by the loan originators. This number must not be listed in either the buyer's or seller's column.

Line 802 is used to record ''Your charge or credit for the specific interest rate chosen,'' which states the charge or credit adjustment as applied to ''Our Service Charge,'' if applicable. This number must not be listed in either column or shown on page one of the HUD–1.

Line 803 is used to record ''Your Adjusted Origination Charges,'' which states the net amount of the loan origination charges. This number must be listed in either the buyer's column or as ''paid outside closing.''

Lines 804–811 may be used to record each of the ''Required services that we select''. Each settlement service provider must be identified by name and the amount paid recorded inside the columns or ''P.O.C.''.

Lines 808–811 may also be used to record other required lender or loan program disclosures. In such a case, any charge must be listed outside the columns.

* * * * *

Lines 1000–1009. * * *

After itemizing individual deposits in the 1000 series, the servicer shall make an adjustment based on aggregate accounting. This adjustment equals the difference between the deposit required under aggregate accounting and the sum of the itemized deposits. The computation steps for aggregate accounting are set out in § 3500.17(d). The adjustment will always be a negative number or zero (-0-). The settlement agent shall enter the aggregate adjustment amount on a final line of the 1000 series of the HUD–1 or HUD–1A statement.

Lines 1100–1115. This series covers title charges and charges by attorneys. The title charges include a variety of services performed by title companies or others, and include fees directly related to the transfer of title (title examination, title search, document preparation) and fees for title insurance. The legal charges include fees for Lender's, Seller's, or Buyer's attorney, or the attorney preparing title work. The series also includes any settlement, notary, or delivery fees.

Line 1101 is used to record the total for the category of ''Title services and lender's title insurance,'' and the amount must be listed in the columns.

Lines 1102–1108 may be used to itemize charges paid other than those defined as ''primary title services,'' such as for a closing attorney or escrow agent, and those charges paid must be listed outside the columns. Lines 1102–1108 may also be used to itemize some required title services whose costs are already included in Line 1101. In such a case, any charge must be listed outside the columns.

Line 1109 is used to record ''Lender's title insurance premium,'' and the amount must be listed outside the columns.

Line 1110 is used to record ''Optional owner's title insurance,'' and the amount must be listed in the columns.

Line 1111 is used to record the lender's title insurance policy limits of coverage, and the amount must be listed outside the columns.

Line 1112 is used to record the owner's title insurance policy limits of coverage, and the amount must be listed outside the columns.

Line 1113 is used to record the title agent's portion of the total title insurance premium, and the amount must be listed outside the columns.

Line 1114 is used to record the underwriter's portion of the title insurance premium, and the amount must be listed outside the columns.

Line 1201 is used to record the total ''Government recording and transfer charges,'' and the amount must be listed in the columns.

Lines 1202–1205 may be used to record specific itemized third party charges for government recording and transfer services, but the amounts must be listed outside the columns.

Lines 1301–1305 may be used to record additional itemized settlement charges, and the amounts must be listed in either column.

Line 1400 must state the total settlement charges stated within each column.

Line Item Instructions for Completing HUD–1A

Note: The HUD–1A, including the closing script addendum, is an optional form that may be used for refinancing and subordinate lien federally related mortgage loans, as well as for any other one-party transaction that does not involve the transfer of title to residential real property.[34] * * *

* * * * *

General Instructions for Completing Closing Script Addendum to HUD–1/1A Settlement Form

The settlement agent must complete the closing script addendum to the HUD–1/1A settlement form pursuant to § 3500.8(d) and in accordance with the instructions and example closing script forms contained in this Appendix A.

BILLING CODE 4210–67–P

[34] Note the HUD–1A and its instructions will be conformed to changes to the HUD–1 and HUD–1 instructions at the final rule stage.

A. **Settlement Statement**

U.S. Department of Housing and Urban Development

OMB Approval No. 2502-0265 (expires 11/30/2009)

B. Type of Loan			
1 ☐ FHA 2 ☐ FmHA 3 ☐ Conv. Unins. 4. ☐ VA 5. ☐ Conv. Ins.	6 File Number	7 Loan Number	8 Mortgage Insurance Case Number.

C. Note: This form is furnished to give you a statement of actual settlement costs Amounts paid to and by the settlement agent are shown. Items marked "(p.o.c.)" were paid outside the closing; they are shown here for informational purposes and are not included in the totals.

D. Name & Address of Borrower	E. Name & Address of Seller	F Name & Address of Lender

G Property Location	H Settlement Agent	
	Place of Settlement	I Settlement Date:

J. Summary of Borrower's Transaction		K. Summary of Seller's Transaction	
100. Gross Amount Due From Borrower		**400. Gross Amount Due To Seller**	
101. Contract sales price		401 Contract sales price	
102. Personal property		402. Personal property	
103. Settlement charges to borrower (line 1400)		403.	
104.		404	
105.		405	
Adjustments for items paid by seller in advance		**Adjustments for items paid by seller in advance**	
106. City/town taxes to		406 City/town taxes to	
107. County taxes to		407 County taxes to	
108. Assessments to		408. Assessments to	
109.		409.	
110.		410.	
111.		411.	
112.		412	
120. Gross Amount Due From Borrower		**420. Gross Amount Due To Seller**	
200. Amounts Paid By Or In Behalf Of Borrower		**500. Reductions In Amount Due To Seller**	
201. Deposit or earnest money		501 Excess deposit (see instructions)	
202 Principal amount of new loan(s)		502 Settlement charges to seller (line 1400)	
203 Existing loan(s) taken subject to		503. Existing loan(s) taken subject to	
204.		504. Payoff of first mortgage loan	
205.		505. Payoff of second mortgage loan	
206.		506.	
207.		507	
208.		508	
209.		509.	
Adjustments for items unpaid by seller		**Adjustments for items unpaid by seller**	
210. City/town taxes to		510 City/town taxes to	
211. County taxes to		511. County taxes to	
212. Assessments to		512. Assessments to	
213		513.	
214.		514.	
215		515.	
216		516.	
217.		517.	
218.		518.	
219.		519	
220. Total Paid By/For Borrower		**520. Total Reduction Amount Due Seller**	
300. Cash At Settlement From/To Borrower		**600. Cash At Settlement To/From Seller**	
301. Gross Amount due from borrower (line 120)		601. Gross amount due to seller (line 420)	
302. Less amounts paid by/for borrower (line 220)	( )	602. Less reductions in amt. due seller (line 520)	( )
303. Cash ☐ From ☐ To Borrower		**603. Cash ☐ To ☐ From Seller**	

Section 5 of the Real Estate Settlement Procedures Act (RESPA) requires the following: • HUD must develop a Special Information Booklet to help persons borrowing money to finance the purchase of residential real estate to better understand the nature and costs of real estate settlement services; • Each lender must provide the booklet to all applicants from whom it receives or for whom it prepares a written application to borrow money to finance the purchase of residential real estate; • Lenders must prepare and distribute with the Booklet a Good Faith Estimate of the settlement costs that the borrower is likely to incur in connection with the settlement. These disclosures are manadatory.

Section 4(a) of RESPA mandates that HUD develop and prescribe this standard form to be used at the time of loan settlement to provide full disclosure of all charges imposed upon the borrower and seller. These are third party disclosures that are designed to provide the borrower with pertinent information during the settlement process in order to be a better shopper.

The Public Reporting Burden for this collection of information is estimated to average one hour per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information.

This agency may not collect this information, and you are not required to complete this form, unless it displays a currently valid OMB control number.

The information requested does not lend itself to confidentiality.

Previous editions are obsolete

Page 1 of 2

This form is also on www.hud.gov/respa

form **HUD-1** (2/07)
ref Handbook 4305.2

L. Settlement Charges	Paid From Borrower's Funds at Settlement	Paid From Seller's Funds at Settlement
700. Total Sales/Broker's Commission based on price $ @ % =		
Division of Commission (line 700) as follows:		
701. $ to		
702. $ to		
703. Commission paid at Settlement		
704		
800. Items Payable In Connection With Loan		
801. ***Our service charge (from GFE #1)*** ***$***		
802. ***Your charge or credit for the specific interest rate chosen (from GFE #2)*** ***$***		
803. ***Your Adjusted Origination Charges (from GFE A)*** ***$***		
804. ***Appraisal fee to (from GFE #3)***		
805. ***Credit report to (from GFE #3)***		
806. ***Tax service (from GFE #3)***		
807. ***Flood certification (from GFE #3)***		
808		
809		
810		
811		
900. Items Required By Lender To Be Paid In Advance		
901. ***Daily interest charges (from GFE #8)*** from to @$ /day		
902. ***Mortgage insurance premium (from GFE #3 or #5)*** for months to		
903. ***Homeowner's insurance (from GFE #9)*** for years to $		
904. years to		
905		
1000. Reserves Deposited With Lender		
1001. ***Reserves or escrow (from GFE #7)***		
1002. Homeowner's insurance months@$ per month $		
1003. Mortgage insurance months@$ per month $		
1004. City property taxes months@$ per month $		
1005. County property taxes months@$ per month $		
1006. Annual assessments months@$ per month $		
1007. months@$ per month $		
1008. months@$ per month $		
1009. Aggregate Adjustment -$		
1100. Title Charges		
1101. ***Title services and lender's title insurance (from GFE #4)***		
1102		
1103		
1104		
1105		
1106		
1107		
1108		
1109. Lender's title insurance premium $		
1110. ***Optional owner's title insurance (from GFE #10)***		
1111. Lender's title policy limits $		
1112. Owner's title policy limits $		
1113. Agent's portion of the total title insurance premium $		
1114. Underwriter's portion of the total title insurance premium $		
1115		
1200. Government Recording and Transfer Charges		
1201. ***Government Recording and Transfer Charges (from GFE #6)***		
1202. Recording fees: Deed $; Mortgage $; Releases $		
1203. City/county tax/stamps: Deed $; Mortgage $		
1204. State tax/stamps: Deed $; Mortgage $		
1205. Conservation fee $		
1206		
1300. Additional Settlement Charges		
1301. ***Survey (from GFE #5)*** to		
1302. ***Pest inspection (from GFE #5)*** to		
1303		
1304		
1305		
1400. Total Settlement Charges (enter on lines 103, Section J and 502, Section K)		

Settlement Statement
Optional Form for
Transactions without Sellers

U.S. Department of Housing and Urban Development

OMB Approval No 2502-0265 (expires 11/30/2009)

Name & Address of Borrower	Name & Address of Lender
Property Location (if different from above)	Settlement Agent
	Place of Settlement
Loan Number	Settlement Date

L. Settlement Charges	
800. Items Payable In Connection with Loan	
801 Loan origination fee % to	
802 Loan discount % to	
803 Appraisal fee to	
804 Credit report to	
805 Inspection fee to	
806 Mortgage insurance application fee to	
807 Mortgage broker fee to	
808	
809	
810	
811	
900. Items Required by Lender to be Paid in Advance	
901 Interest from to @ $ per day	
902 Mortgage insurance premium for months to	
903 Hazard insurance premium for year(s) to	
904	
1000. Reserves Deposited with Lender	
1001 Hazard insurance months @ $ per month	
1002 Mortgage insurance months @ $ per month	
1003 City property taxes months @ $ per month	
1004 County property taxes months @ $ per month	
1005 Annual assessments months @ $ per month	
1006 months @ $ per month	
1007 months @ $ per month	
1008 months @ $ per month	
1100. Title Charges	
1101 Settlement or closing fee to	
1102 Abstract or title search to	
1103 Title examination to	
1104 Title Insurance binder to	
1105 Document preparation to	
1106 Notary fees to	
1107 Attorney's fees to (includes above item numbers)	
1108 Title insurance to (includes above item numbers)	
1109 Lender's coverage $	
1110 Owner's coverage $	
1111	
1112	
1113	
1200. Government Recording and Transfer Charges	
1201 Recording fees	
1202 City/county tax/stamps	
1203 State tax/stamps	
1204	
1205	
1300. Additional Settlement Charges	
1301 Survey to	
1302 Pest inspection to	
1303 Architectural/engineering services to	
1304 Building permit to	
1305	
1306	
1307	
1400. Total Settlement Charges (enter on line 1602)	

M. Disbursement to Others	
1501	
1502	
1503	
1504	
1505	
1506	
1507	
1508	
1509	
1510	
1511	
1512	
1513	
1514	
1515	
1520. TOTAL DISBURSED (enter on line 1603)	

NOTE: This is the current HUD-1A form. This form and its instructions will be revised to conform to the final changes to the HUD-1 and the HUD-1 instructions.

N. NET SETTLEMENT	
1600 Loan Amount	$
1601 **Plus** Cash/Check from Borrower	$
1602 **Minus** Total Settlement Charges (line 1400)	$
1603 **Minus** Total Disbursements to Others (line 1520)	$
1604 **Equals** Disbursements to Borrower (after expiration of any applicable rescission period required by law)	$

Borrower(s) Signature(s)

This form is also on www.hud.gov/respa

X

form **HUD-1A** (2/94)
ref RESPA

Public reporting burden for this collection of information is estimated to average 0 35 hours per response, including the time for reviewing instructions, searching existing data sources, gathering and maintaining the data needed, and completing and reviewing the collection of information. This agency may not collect this information, and you are not required to complete this form, unless it displays a currently valid OMB control number

Instructions for completing form HUD-1A

Note: This form is issued under authority of the Real Estate Settlement Procedures Act (RESPA), 12 U.S.C. 2601 *et seq*. The regulation for RESPA is Regulation X, codified as 24 CFR 3500, and administered by the Department of Housing and Urban Development (HUD). Regulation Z referred to in the next paragraph is the regulation implementing the Truth in Lending Act (TILA), 15 U.S.C. 1601 *et seq.* and codified as 12 CFR part 226.

HUD-1A is an optional form that may be used for refinancing and subordinate lien federally related mortgage loans, as well as for any other one-party transaction that does not involve the transfer of title to residential real property. The HUD-1 form may also be used for such transactions, by utilizing the borrower's side of the HUD-1 and following the relevant parts of the instructions set forth in Appendix A of Regulation X. The use of either the HUD-1 or HUD-1A is not mandatory for open-end lines of credit (home-equity plans), as long as the provisions of Regulation Z are followed.

Background

The HUD-1A settlement statement is to be used as a statement of actual charges and adjustments to be given to the borrower at settlement. The instructions for completion of the HUD-1A are for the benefit of the settlement agent who prepares the statement; the instructions are not a part of the statement and need not be transmitted to the borrower. There is no objection to using the HUD-1A in transactions in which it is not required, and its use in open-end lines of credit transactions (home-equity plans) is encouraged. It may not be used as a substitute for a HUD-1 in any transaction in which there is a transfer of title and a first lien is taken as security.

Refer to the "definitions" section of Regulation X for specific definitions of terms used in these instructions.

General Instructions

Information and amounts may be filled in by typewriter, hand printing, computer printing, or any other method producing clear and legible results. Additional pages may be attached to the HUD-1A for the inclusion of customary recitals and information used locally for settlements or if there are insufficient lines on the HUD-1A.

The settlement agent shall complete the HUD-1A to itemize all charges imposed upon the borrower by the lender, whether to be paid at settlement or outside of settlement, and any other charges that the borrower will pay for at settlement. In the case of "no cost" or "no point" loans, these charges include any payments the lender will make to affiliated or independent settlement service providers relating to this settlement. These charges shall be included on the HUD-1A, but marked "P.O.C." for "paid outside of closing," and shall not be used in computing totals. Such charges also include indirect payments or back-funded payments to mortgage brokers that arise from the settlement transaction. When used, "P.O.C." should be placed in the appropriate lines next to the identified item, ***not in the columns themselves.***

Blank lines are provided in Section L for any additional settlement charges. Blank lines are also provided in Section M for recipients of all or portions of the loan proceeds. The names of the recipients of the settlement charges in Section L and the names of the recipients of the loan proceeds in Section M should be set forth on the blank lines.

Line item instructions

The identification information at the top of the HUD-1A should be completed as follows:

The borrower's name and address is entered in the space provided. If the property securing the loan is different from the borrower's address, the address or other location information on the property should be entered in the space provided. The loan number is the lender's identification number for the loan. The settlement date is the date of settlement in accordance with § 3500.2 of Regulation X, not the end of any applicable rescission period. The name and address of the lender should be entered in the space provided.

Section L. Settlement Charges. This section of the HUD-1A is similar to section L of the HUD-1, with the deletion of lines 700 through 704, relating to real estate broker commissions. The Instructions for filling out the HUD-1 as set forth in Appendix A of Regulation X provide additional information regarding Section L, if needed.

Line 1400 in the HUD-1A is for the total settlement charges charged to the borrower. Enter this total on line 1602 as well. This total should include Section L amounts from additional pages, if any are attached to this HUD-1A.

Section M. Disbursement to Others. This section is used to list payees, other than the borrower, of all or portions of the loan proceeds (including the lender, if the loan is paying off a prior loan made by the same lender), when the payee will be paid directly out of the settlement proceeds. It is not used to list payees of settlement charges, nor to list funds disbursed directly to the borrower, even if the lender knows the borrower's intended use of the funds.

For example, in a refinancing transaction, the loan proceeds are used to pay off an existing loan. The name of the lender for the loan being paid off and the pay-off balance would be entered in Section M. In a home improvement transaction when the proceeds are to be paid to the home improvement contractor, the name of the contractor and the amount paid to the contractor would be entered in Section M. In a consolidation loan, or when part of the loan proceeds is used to pay off other creditors, the name of each creditor and the amount paid to that creditor would be entered in Section M. If the proceeds are to be given directly to the borrower and the borrower will use the proceeds to pay off existing obligations, this would not be reflected in Section M.

Section N. Net Settlement. Line 1600 normally sets forth the principal amount of the loan as it appears on the related note for this loan. In the event this form is used for an open-ended home equity line whose approved amount is greater than the initial amount advanced at settlement, the amount shown on Line 1600 will be the loan amount advanced at settlement. Line 1601 is used for all settlement charges that are both included in the totals for lines 1400 and 1602 and are not financed as part of the principal amount of the loan. This is the amount normally received by the lender from the borrower at settlement, which would occur when some or all of the settlement charges were paid in cash by the borrower at settlement, instead of being financed as part of the principal amount of the loan. Failure to include any such amount in line 1601 will result in an error in the amount calculated on line 1604. P.O.C. amounts should not be included in line 1601.

Line 1602 is the total amount from line 1400.

Line 1603 is the total amount from line 1520.

Line 1604 is the amount disbursed to the borrower. This is determined by adding together the amounts for lines 1600 and 1601, and then subtracting any amounts listed on lines 1602 and 1603.

INSTRUCTIONS TO CLOSING SCRIPT PREPARER

The Closing Script is comprised of nine categories: Introduction, Loan Description, Interest Rate, Payment, Late Payment, Prepayment Penalty, Balloon Loan, Closing Costs, and Acknowledgment.

Each category in this document contains clauses that are required in preparing a Closing Script specific to each purchase or refinance loan.

The clauses should appear in the Closing Script in the same categorical order as listed in this instructional document.

All clauses that contain information in bold typeset must remain in bold typeset and all blank spaces in the selected clauses must be completed with the borrower's specific loan information.

The party preparing the Closing Script must complete the Closing Script with information provided by the loan originator, contained in the Good Faith Estimate (GFE), the Lender's General and Specific Closing Instructions, the Note, the Deed of Trust or Mortgage, and any other instrument(s) securing the loan.

Introduction (include in all Closing Scripts)

The following paragraph introduces the Closing Script to the borrower(s). It must be used in all Closing Scripts.

THESE ARE YOUR LOAN DETAILS

The following is a summary of many important details involving the mortgage loan for <u>(PROPERTY ADDRESS)</u>. Let's compare these important details with the Good Faith Estimate (GFE), loan documents, and other disclosures.

Loan Description (include in all Closing Scripts)

The Loan Amount must state the total loan amount as evidenced in the Note.
The Loan Term must state in months or years the length of the loan.
The Loan Type must state the following:

- If the loan is Conventional, FHA, VA, or other government program.
- If the loan is a Fixed Rate, Adjustable Rate, Hybrid Adjustable, Payment Option Mortgage or other such description that correctly identifies the loan product.

Loan Amount	Loan Term	Loan Type
$ ________	________	____________

Interest Rate (Chose one of the following)

Fixed Interest Rate

Your loan has a fixed interest rate of ____%.

A fixed interest rate means that your interest rate will not rise over the life of the loan.

Adjustable Rate Mortgage

Your initial interest rate is _____%.

Your loan has an adjustable interest rate, which means that the interest rate can rise over the life of the loan.

Your first interest rate adjustment or change date is _______________ and may change every ___________ thereafter. Your interest rate can increase or decrease by _____ on every change date, but will never be lower than _____% or higher than ______% over the life of the loan.

Adjustable Interest Rate with Initial Discounted Interest Rate

Your initial interest rate is _______%. This is a discounted interest rate and will adjust to ______% in _____(days/months) on (DATE).

Your loan has an adjustable interest rate which means that the interest rate can rise over the life of the loan.

Your second change date will be **(DATE)** and may change every _________ thereafter. Your interest rate can increase or decrease by _______ % on every change date, but will never be lower than _______ % or higher than _______ % over the life of the loan.

Hybrid Adjustable Rate Mortgage

Your loan is a hybrid adjustable rate mortgage.

You have an initial fixed interest rate of ______%. As long as your interest rate remains fixed, your interest rate will not rise.

Your initial fixed interest rate will change to an adjustable rate mortgage on the first change date, ______________. The adjustable interest rate may change every __________ thereafter. Your interest rate can increase or decrease by ____ % on every change date, but will never be lower than _____% or higher than ______% over the life of the loan.

When your loan changes from a fixed interest rate to an adjustable interest rate, your interest rate can rise.

Payment (Choose one of the following)

(Fixed Rate – With Escrow Account)

Payment

Your loan payment for principal and interest (**$**________) and mortgage insurance (**$**________) is **$**__________ and **can/cannot** rise.

- AND -

You have an escrow account. In addition to any mortgage insurance, your initial escrow payment is **$**_______ for (*INSERT THE TYPE OF ALL ESCROWED ITEMS SUCH AS PROPERTY TAXES OR HOMEOWNERS INSURANCE INTO THE FOLLOWING BLANKS. DO NOT INCLUDE MORTGAGE INSURANCE. ADDITIONAL BLANKS MAY BE ADDED AND EXTRA BLANKS MAY BE REMOVED*) _____________, ______________, and __________________. This amount may increase.

Your total payment is **$**________ for principal*, interest, any mortgage insurance, (*INSERT THE TYPE OF ALL ESCROWED ITEMS SUCH AS PROPERTY TAXES OR HOMEOWNERS INSURANCE INTO THE FOLLOWING BLANKS. ADDITIONAL BLANKS MAY BE ADDED AND EXTRA BLANKS MAY BE REMOVED*) _____________, ______________, and __________________.

*Omit principal if loan is interest-only.

- OR -

(Fixed Rate – No Escrow Account)

Payment

Your loan payment for principal and interest (**$**________) and mortgage insurance (**$**________) is **$**__________ and **can/cannot** rise.

- AND -

You do not have an escrow account. Any and all items such as property taxes and homeowners insurance must be paid directly by you.

Your total payment is **$**________ for principal, interest, and any mortgage insurance.

- OR –

(Adjustable Interest Rate, Adjustable Interest Rate with Initial Discounted Rate or Hybrid Adjustable Interest Rate - With Escrow Account)

Payment

Your initial loan payment for principal and interest (**$________**) and mortgage insurance (**$________**) is **$__________** and **can rise**.

- AND -

The highest your principal and interest payment can reach, based on the maximum interest rate of ______**%** is **$_________**. The earliest it can reach this is _______________.

You have an escrow account. In addition to any mortgage insurance, your initial escrow payment is **$_______** for (*INSERT THE TYPE OF ALL ESCROWED ITEMS SUCH AS PROPERTY TAXES OR HOMEOWNERS INSURANCE INTO THE FOLLOWING BLANKS. DO NOT INLCUDE MORTGAGE INSURANCE. ADDITIONAL BLANKS MAY BE ADDED AND EXTRA BLANKS MAY BE REMOVED*) _____________, ______________, and __________________. This amount may increase.

Your total initial payment is **$________** for principal, interest, any mortgage insurance (*INSERT THE TYPE OF ALL ESCROWED ITEMS SUCH AS PROPERTY TAXES OR HOMEOWNERS INSURANCE INTO THE FOLLOWING BLANKS. DO NOT INCLUDE MORTGAGE INSURANCE. ADDITIONAL BLANKS MAY BE ADDED AND EXTRA BLANKS MAY BE REMOVED*) _____________, ______________, and __________________.

- OR -

(Adjustable Interest Rate, Adjustable Interest Rate with Initial Discounted Rate or Hybrid Adjustable Interest Rate – No Escrow Account)

Payment

Your initial loan payment for principal and interest (**$________**) and mortgage insurance (**$________**) is **$__________** and **can rise**.

- AND -

The highest your principal and interest payment can reach, based on the maximum interest rate of ______**%** is **$_________**. The earliest it can reach this is _______________.

You do not have an escrow account. Any and all items such as property taxes and homeowners insurance must be paid directly by you.

Your total initial payment is **$________** for principal, interest, and any mortgage insurance.

Additional Payment Clauses (insert if applicable)

Interest-Only Mortgage

(*INSERT THE INTEREST-ONLY CLAUSE, WHEN APPLICABLE, AND REPLACE THE FIRST SENTENCE IN THE PAYMENT CATEGORY CLAUSE.*)

Your loan payment for interest (**$_______**) and mortgage insurance (**$_______**) is **$________** and **can/cannot rise**. This will not reduce the principal balance of your loan.

Payment Option Mortgage

This type of loan allows you to choose from three payment options: the traditional principal and interest payment, the interest-only payment, and the minimum interest payment. This is what your initial payment choice will look like:

Principal & Interest Payment at ____%: $_______
(reduces loan balance) $______ principal, $______ interest

Interest-Only Payment at _____%: $_______
(will not reduce loan balance) $0 principal, $______ interest

Minimum Interest Payment at ____%: $_______
(will INCREASE loan balance) $0 principal, $______ interest

AND $_______ is added to your loan balance

If you choose to pay the minimum interest payment, your loan balance will increase. This increase instead of a decrease in your loan balance is called negative amortization. If the loan balance increases, your monthly mortgage payment will also increase to cover the difference.

If your loan balance rises above _____%, as indicated in your Note, your lender has the right to increase your loan payments greatly for the remainder of the loan.

Late Payment (include in all Closing Scripts)

Your loan payment is due on the ____ of every month and is considered late after the ____ of every month. If your lender receives your mortgage payment after the _____, your lender will charge a late fee of _____**%** of the overdue payment of principal and interest.

*If loan payment terms are other than monthly, modify accordingly.

Loan Balance (choose one of the following)

Your loan balance cannot rise.

- OR -

Loan Balance

Your loan balance **can rise to a maximum of $ ____________.**

Prepayment Penalty (choose one of the following)

Prepayment Penalty

You **do not have** a pre-payment penalty.

- OR -

Prepayment Penalty

You **have** a pre-payment penalty.

A prepayment penalty is an additional amount that you will be required to pay if you pay your loan off early such as through the sale of your home, refinancing your loan, or if you make significant additional payments to principal prior to **(DATE)**. Based on your initial loan amount, your prepayment penalty may be as high as **$**____________.

Balloon Loan (choose one of the following)

You **do not have** a balloon payment.

- OR -

Balloon Payment

Your loan has a balloon payment. At the end of the loan term, any balance remaining will have to be paid. In the case of a balloon loan, often very little, if any, of the loan balance is paid down, therefore, the last payment, the balloon payment can be most of the initial loan balance. Most consumers with a balloon note refinance their loan before the final balloon payment becomes due.

Your balloon payment will become due on **(DATE)** in the amount of **$**_____________.

Closing Costs (include in all Closing Scripts)

Closing Costs

Next we will review all of the HUD-1/1A charges and credits associated with your loan and compare them to the GFE you received when you applied for this loan.

Preparation of the GFE & HUD-1/1A Actual Charges Comparison Chart

The Comparison Chart is to be prepared using the exact information and amounts from the GFE and the actual settlement charges shown on the HUD-1/1A Settlement Statement.

The Comparison Chart is comprised of three categories: Charges Cannot Increase, Charges Cannot Increase More Than 10%, and Charges Can Change, and three columns; Good Faith Estimate, HUD-1/1A, and $ Increase.

GFE Instructions:

All information and amounts from the borrower's GFE numbered 1, 2, and 6 must be entered in the Charges Cannot Increase category in the GFE column.

All information and amounts from the borrower's GFE numbered 3, 4, 5, and 10 must be entered in the Charges Cannot Increase More Than 10% category in the GFE column **IF** these are services required or identified by the loan originator. Additional lines may be added.

All information and amounts from the borrower's GFE numbered 3, 4, 5, and 10 must be entered in the Charges Can Change category in the GFE column **IF** these are services selected by the borrower. Additional lines may be added.

HUD-1/1A Instructions:

All information and amounts obtained from the HUD-1/1A must be entered into the HUD-1/1A column in the same category that corresponds to the information/amount obtained from the borrower's GFE. Additional lines may be added to the Charges Cannot Increase More Than 10% and the Charges Can Change categories.

$ Increase Instructions:

Charges Cannot Increase Category – Any increases in any line items in the GFE and the HUD-1/1A columns must be shown numerically. Each increase must be listed separately and not totaled.

Charges Cannot Increase More Than 10% – The sum of all line items shown in this category must be entered in numerical format totaled and calculated as a percentage increase.

Charges Can Change – No information is required to be entered into this column for this category, but may be listed voluntarily.

GFE & HUD-1/1A Charges Comparison Chart

	Good Faith Estimate	HUD-1/1A	$ Increase
Charges Cannot Increase			
Our service charge (HUD-1/1A Line #801)			
Your credit or charge for the specific interest rate chosen (HUD-1/1A Line #802)			
Your Adjusted Origination Charges (HUD-1/1A Line #803)			
Government recording and transfer charges (HUD-1/1A Line #1201)			
Charges Cannot Increase More Than 10%			
Appraisal (HUD-1/1A Line #804)			
Credit Report (HUD-1/1A Line #805)			
Tax service (HUD-1/1A Line #806)			
Flood certification (HUD-1/1A Line #807)			
Mortgage Insurance Premium (HUD-1/1A Line #902)			
________ (HUD-1/1A Line #____)			
________ (HUD-1/1A Line #____)			
________ (HUD-1/1A Line #____)			
Total			
***Increase between GFE and HUD-1/1A Charges**		%	
Charges Can Change			
Reserves or escrow (HUD-1/1A Line #1001)			
Daily interest charges (HUD-1/1A Line #901) $______ per day			
Homeowners insurance (HUD-1/1A Line #903)			
________ (HUD-1/1A Line #____)			
________ (HUD-1/1A Line #____)			
________ (HUD-1/1A Line #____)			

Acknowledgment (include in all Closing Scripts)

The acknowledgment must be signed and dated by the party conducting the closing and all borrowers.

Acknowledgment

The undersigned hereby state that the Closing Script was read and the following information was provided and explained:

1. The comparison between the charges listed on the HUD-1/1A settlement form and the estimate of charges on the GFE;
2. Whether or not the tolerances have been met within the applicable categories between the GFE and the HUD-1/1A; and
3. Any inconsistencies between the loan documents (including the mortgage note) and the summary of the loan terms on the GFE, and between the HUD-1/1A settlement charges and the charges stated on the GFE.

__________________ (Representative) __________________ (Company)

__________________ (Borrower) __________________ (Borrower)

__________________ (Date)

EXAMPLES OF COMPLETED CLOSING SCRIPTS

Example 1 – Fixed Interest Rate Mortgage

THESE ARE YOUR LOAN DETAILS

The following is a summary of many important details involving the mortgage loan for 123 Main Street, Hometown, USA 00000. Let's compare these important details with the Good Faith Estimate (GFE), loan documents, and other disclosures.

Loan Amount	Loan Term	Loan Type
$300,000.00	30 year	FHA Insured Fixed Rate

Fixed Interest Rate

Your loan has a fixed interest rate of **6.5%**.

A fixed interest rate means that your interest rate will not rise over the life of the loan.

Payment

Your loan payment for principal and interest (**$1,896.20**) and mortgage insurance (**$62.00**) is **$1,958.20** and **cannot** rise.

You have an escrow account. In addition to any mortgage insurance, your initial escrow payment is **$200.00** for property taxes and homeowners insurance. This amount may increase.

Your total payment is $**2,158.20** for principal, interest, any mortgage insurance, property taxes and homeowners insurance.

Late Payment

Your loan payment is due on the 1st of every month and is considered late after the 15th of every month. If your lender receives your mortgage payment after the 15th, your lender will charge a late fee of **5%** of the overdue payment of principal and interest.

Loan Balance

Your loan balance **cannot** rise.

Prepayment Penalty

You **do not have** a prepayment penalty.

Balloon Payment

You **do not have** a balloon payment.

Closing Costs

Next we will review all of the HUD-1/1A charges and credits associated with your loan and compare them to the GFE you received when you applied for this loan.

GFE & HUD-1/1A Charges Comparison Chart

	Good Faith Estimate	HUD-1/1A	$ Increase
Charges Cannot Increase			
Our service charge (HUD-1/1A Line #801)	$6,000.00	$6,000.00	0
Your credit or charge for the specific interest rate chosen (HUD-1/1A Line #802)	-$4,000.00	-$4,000.00	0
Your Adjusted Origination Charges (HUD-1/1A Line #803)	$2,000.00	$2,000.00	0
Government recording and transfer charges (HUD-1/1A Line #1201)	$1,250.00	$1,250.00	0
Charges Cannot Increase More Than 10%			
Appraisal (HUD-1/1A Line #804)	$300.00	$300.00	
Credit Report (HUD-1/1A Line #805)	$40.00	$23.00	
Tax service (HUD-1/1A Line #806)	$70.00	$70.00	
Flood certification (HUD-1/1A Line #807)	$12.00	$12.00	
Mortgage Insurance Premium (HUD-1/1A Line #902)	$62.00	$62.00	
Survey ____________ (HUD-1/1A Line #1301)	$175.00	$145.00	
Pest Inspection ____________ (HUD-1/1A Line #1302)	$45.00	$45.00	
____________ (HUD-1/1A Line #____)			
Total	**$704.00**	**$657.00**	
***Increase between GFE and HUD-1/1A Charges**	**0%**		
Charges Can Change			
Reserves or escrow (HUD-1/1A Line #1001)	$262.00	$262.00	
Daily interest charges (HUD-1/1A Line #901) $53.42 per day	$53.42	$106.84	
Homeowners insurance (HUD-1/1A Line #903)	$600.00	$610.00	
Title services and lender's title insurance (HUD-1/1A Line #1101)	$975.00	$975.00	
Optional owner's title insurance (HUD-1/1A Line #1110)	$725.00	$725.00	
____________ (HUD-1/1A Line #____)			

Acknowledgment

The undersigned hereby state that the Closing Script was read and the following information was provided and explained:

1. The comparison between the charges listed on the HUD-1/1A settlement form and the estimate of charges on the GFE;
2. Whether or not the tolerances have been met within the applicable categories between the GFE and the HUD-1/1A; and
3. Any inconsistencies between the loan documents (including the mortgage note) and the summary of the loan terms on the GFE, and between the HUD-1/1A settlement charges and the charges stated on the GFE.

__________________ (Representative) __________________ (Company)

__________________ (Borrower) __________________ (Borrower)

__________________ (Date)

Example 2 – Adjustable Rate Mortgage

THESE ARE YOUR LOAN DETAILS

This is a summary of many important details involving the mortgage loan for 123 Main Street, Hometown, USA 00000. Let's compare these important details with the Good Faith Estimate (GFE), loan documents, and other disclosures.

Loan Amount	Loan Term	Loan Type
$300,000.00	**30 year**	**Conventional Adjustable Rate**

Adjustable Rate Mortgage

Your initial interest rate is **6.5%**

Your loan has an adjustable interest rate, which means that the interest rate can rise over the life of the loan.

Your first interest rate adjustment or change date is **January 1, 2008** and may change every **12 months** thereafter. Your interest rate can increase or decrease by **2.0%** on every change date, but will never be lower than **4.5%** or higher than **10.5%** over the life of the loan.

Payment

Your initial loan payment for principal and interest **($1,896.20)** and mortgage insurance **($0)** is **$1,896.20** and **can rise**.

The highest your principal and interest payment can reach, based on the maximum interest rate of **10.5%** is $**2,744.22.** The earliest it can reach this is **January 1, 2010.**

You do not have an escrow account. Any and all items such as property taxes and homeowners insurance must be paid directly by you.

Your total initial payment is $**1,896.20** for principal, interest, and any mortgage insurance.

Late Payment

Your loan payment is due on the 1st of every month and is considered late after the 15th of every month. If your lender receives your mortgage payment after the 15th, your lender will charge a late fee of **5%** of the overdue payment of principal and interest.

Loan Balance

Your loan balance **cannot** rise.

Prepayment Penalty

You **have** a pre-payment penalty.

A prepayment penalty is an additional amount that you will be required to pay if you pay your loan off early such as through the sale of your home, refinancing your loan, or if you make significant additional payments to principal prior **June 1, 2010**. Based on your initial loan amount, your prepayment penalty may be as high as **$9,400.00**.

Balloon Payment

You **do not have** a balloon payment.

Closing Costs

Next we will review all of the HUD-1/1A charges and credits associated with your loan and compare them to the GFE you received when you applied for this loan.

GFE & HUD-1/1A Charges Comparison Chart

	Good Faith Estimate	HUD-1/1A	$ Increase
Charges Cannot Increase			
Our service charge (HUD-1/1A Line #801)	$6,000.00	$6,000.00	0
Your credit or charge for the specific interest rate chosen (HUD-1/1A Line #802)	-$4,000.00	-$4,000.00	0
Your Adjusted Origination Charges (HUD-1/1A Line #803)	$2,000.00	$2,000.00	0
Government recording and transfer charges (HUD-1/1A Line #1201)	$1,250.00	$1,250.00	0
Charges Cannot Increase More Than 10%			
Appraisal (HUD-1/1A Line #804)	$300.00	$350.00	
Credit Report (HUD-1/1A Line #805)	$40.00	$45.00	
Tax service (HUD-1/1A Line #806)	$70.00	$85.00	
Flood certification (HUD-1/1A Line #807)	$12.00	$15.00	
Mortgage Insurance Premium (HUD-1/1A Line #902)			
Survey ____________ (HUD-1/1A Line #1301)	$175.00	$175.00	
Pest Inspection ____________ (HUD-1/1A Line #1302)	$45.00	$45.00	
____________ (HUD-1/1A Line #____)			
Total	**$642.00**	**$715.00**	**+78**
***Increase between GFE and HUD-1/1A Charges**	**12%**		
Charges Can Change			
Reserves or escrow (HUD-1/1A Line #1001)	$262.00	$262.00	
Daily interest charges (HUD-1/1A Line #901) $53.42 per day	$213.69	$427.36	
Homeowners insurance (HUD-1/1A Line #903)	$600.00	$700.00	
Title services and lender's title insurance (HUD-1/1A Line #1101)	$975.00	$1,075.00	
Optional owner's title insurance (HUD-1/1A Line #1110)	$725.00	$725.00	
____________ (HUD-1/1A Line #____)			

Acknowledgment

The undersigned hereby state that the Closing Script was read and the following information was provided and explained:

1. The comparison between the charges listed on the HUD-1/1A settlement form and the estimate of charges on the GFE;

2. Whether or not the tolerances have been met within the applicable categories between the GFE and the HUD-1/1A; and
3. Any inconsistencies between the loan documents (including the mortgage note) and the summary of the loan terms on the GFE, and between the HUD-1/1A settlement charges and the charges stated on the GFE.

__________________ (Representative) __________________ (Company)

__________________ (Borrower) __________________ (Borrower)

__________________ (Date)

Example 3 – Adjustable Interest Rate with Initial Discounted Interest Rate

THESE ARE YOUR LOAN DETAILS

The following is a summary of many important details involving the mortgage loan for 123 Main Street, Hometown, USA 00000. Let's compare these important details with the Good Faith Estimate (GFE), loan documents, and other disclosures.

Loan Amount	Loan Term	Loan Type
$300,000.00	**30 years**	**Conventional Adjustable Payment Option Mortgage**

Adjustable Interest Rate with Initial Discounted Interest Rate

Your initial interest rate is 1.5%. This is a discounted interest rate and will adjust to 6.5% in 30 days on June 1, 2007.

Your loan has an adjustable interest rate which means that the interest rate can rise over the life of the loan.

Your second change date will be **June 1, 2008** and may change every **12 months** thereafter. Your interest rate can increase or decrease by **2.75%** on every change date, but will never be lower than **4.5%** or higher than **10.5%** over the life of the loan.

Payment

Your initial loan payment for principal and interest (**$1,035.36**) and mortgage insurance (**$0**) is **$1,035.36** and **can rise**.

The highest your principal and interest payment can reach, based on the maximum interest rate of **10.5%** is **$3,644.95**. The earliest it can reach this is **June 1, 2013**.

You do not have an escrow account. Any and all items such as property taxes and homeowners insurance must be paid directly by you.

Your total initial payment is **$1,035.36** for principal, interest, and any mortgage insurance.

Payment Option Mortgage

This type of loan allows you to choose from three payment options: the traditional principal and interest payment, the interest-only payment, and the minimum interest payment. This is what your initial payment choice will look like:

Principal & Interest Payment at 6.5%:	$1,896.20		
(reduces loan balance)		$271.20 principal,	$1,625.00 interest
Interest,Only Payment at 6.5%:	$1,625.00		
(will not reduce loan balance)		0 principal,	$1625.00 interest
Minimum Interest Payment at 4.5%:	$1,125.00,		
(will INCREASE loan balance)		$0 principal,	$1,125.00 interest
AND	**$500.00 is added to your loan balance**.		

If you choose to pay the minimum payment amount, your loan balance will increase. This increase instead of a decrease in your loan balance is called negative amortization. If the loan balance increases, your monthly mortgage payment may also increase to cover the difference.

If your loan balance rises above 125%, as indicated in your Note, your lender has the right to increase your loan payments greatly for the remainder of the loan.

Late Payment

Your loan payment is due on the 1st of every month and is considered late after the 15th of every month. If your lender receives your mortgage payment after the 15th, your lender will charge a late fee of **5%** of the overdue payment of principal and interest.

Loan Balance

Your loan balance **can rise to a maximum of $375,000**.

Prepayment Penalty

You **have** a pre-payment penalty.

A prepayment penalty is an additional amount that you will be required to pay if you pay your loan off early such as through the sale of your home, refinancing your loan, or if you make significant additional payments to principal prior to **June 1, 2010**. Based on your initial loan amount, your prepayment penalty may be as high as **$9,400.00**.

Balloon Payment

You **do not have** a balloon payment.

Closing Costs

Next we will review all of the HUD-1/1A charges and credits associated with your loan and compare them to the GFE you received when you applied for this loan.

GFE & HUD-1/1A Charges Comparison Chart

	Good Faith Estimate	HUD-1/1A	$ Increase
Charges Cannot Increase			
Our service charge (HUD-1/1A Line #801)	$6,000.00	$6,000.00	0
Your credit or charge for the specific interest rate chosen (HUD-1/1A Line #802)	-$4,000.00	-$4,000.00	0
Your Adjusted Origination Charges (HUD-1/1A Line #803)	$2,000.00	$2,000.00	0
Government recording and transfer charges (HUD-1/1A Line #1201)	$1,250.00	$1,250.00	0
Charges Cannot Increase More Than 10%			
Appraisal (HUD-1/1A Line #804)	$300.00	$425.00	
Credit Report (HUD-1/1A Line #805)	$40.00	$45.00	
Tax service (HUD-1/1A Line #806)	$70.00	$85.00	
Flood certification (HUD-1/1A Line #807)	$12.00	$15.00	
Mortgage Insurance Premium (HUD-1/1A Line #902)			
Title services and lender's title insurance (HUD-1/1A Line #1101)	$975.00	$975.00	
Optional owner's title insurance (HUD-1/1A Line #1110	$725.00	$725.00	
Pest Inspection ______ (HUD-1/1A Line #1302)	$35.00	$55.00	
Total	**$2157.00**	**$2325.00**	**+168**
***Increase between GFE and HUD-1/1A Charges**	**8%**		
Charges Can Change			
Reserves or escrow (HUD-1/1A Line #1001)	$262.00	$262.00	
Daily interest charges (HUD-1/1A Line #901) $53.42 per day	$213.69	$427.36	
Homeowners insurance (HUD-1/1A Line #903)	$600.00	$600.00	
Survey ______ (HUD-1/1A Line #1301)	$150.00	$195.00	
______ (HUD-1/1A Line #____)			
______ (HUD-1/1A Line #____)			

Acknowledgment

The undersigned hereby state that the Closing Script was read and the following information was provided and explained:

1. The comparison between the charges listed on the HUD-1/1A settlement form and the estimate of charges on the GFE;
2. Whether or not the tolerances have been met within the applicable categories between the GFE and the HUD-1/1A; and
3. Any inconsistencies between the loan documents (including the mortgage note) and the summary of the loan terms on the GFE, and between the HUD-1/1A settlement charges and the charges stated on the GFE.

__________________ (Representative) ___________________ (Company)

__________________ (Borrower) ___________________(Borrower)

__________________ (Date)

Example 4 – Hybrid Fixed Rate Adjustable Rate Mortgage

THESE ARE YOUR LOAN DETAILS

The following is a summary of many important details involving the mortgage loan for 123 Main Street, Hometown, USA 00000. Let's compare these important details with the Good Faith Estimate (GFE), loan documents, and other disclosures.

Loan Amount	Loan Term	Loan Type
$300,000.00	**30 year**	**Conventional Hybrid Adjustable Rate Mortgage**

Hybrid Adjustable Rate Mortgage

Your loan is a hybrid adjustable rate mortgage.

You have an initial fixed interest rate of **6.5%**. As long as your interest rate remains fixed, your interest rate will not rise.

Your initial fixed interest rate will change to an adjustable rate mortgage on the first change date, **June 1, 2009**. The adjustable interest rate may change every **12 months** thereafter. Your interest rate can increase or decrease by **2.0%** on every change date, but will never be lower than **4.5%** or higher than **10.5%** over the life of the loan.

When your loan changes from a fixed interest rate to an adjustable interest rate, your interest rate can rise.

Payment

Your initial loan payment for principal and interest (**$1,896.20**) and mortgage insurance (**$0**) is **$1,896.20** and **can rise**.

The highest your principal and interest payment can reach, based on the maximum interest rate of **10.5%** is **$2,744.22**. The earliest it can reach this is **January 1, 2011**.

You do not have an escrow account. Any and all items such as property taxes and homeowners insurance must be paid directly by you.

Your total initial payment is **$1,896.20** for principal, interest, and any mortgage insurance.

Late Payment

Your loan payment is due on the 1st of every month and is considered late after the 15th of every month. If your lender receives your mortgage payment after the 15th, your lender will charge a late fee of **5%** of your loan payment.

Loan Balance

Your loan balance **cannot** rise.

Prepayment Penalty

You **have** a pre-payment penalty.

A prepayment penalty is an additional amount that you will be required to pay if you pay your loan off early such as through the sale of your home, refinancing your loan, or if you make significant additional payments to principal prior to **June 1, 2010**. Based on your initial loan amount, your prepayment penalty may be as high as **$9,400.00**.

Balloon Payment

You **do not have** a balloon payment.

Closing Costs

Next we will review all of the HUD-1/1A charges and credits associated with your loan and compare them to the GFE you received when you applied for this loan.

GFE & HUD-1/1A Charges Comparison Chart

	Good Faith Estimate	HUD-1/1A	$ Increase
Charges Cannot Increase			
Our service charge (HUD-1/1A Line #801)	$6,000.00	$6,000.00	0
Your credit or charge for the specific interest rate chosen (HUD-1/1A Line #802)	-$4,000.00	-$4,000.00	0
Your Adjusted Origination Charges (HUD-1/1A Line #803)	$2,000.00	$2,000.00	0
Government recording and transfer charges (HUD-1/1A Line #1201)	$1,250.00	$1,250.00	0
Charges Cannot Increase More Than 10%			
Appraisal (HUD-1/1A Line #804)	$295.00	$325.00	
Credit Report (HUD-1/1A Line #805)	$21.00	$21.00	
Tax service (HUD-1/1A Line #806)	$70.00	$75.00	
Flood certification (HUD-1/1A Line #807)	$12.00	$15.00	
Mortgage Insurance Premium (HUD-1/1A Line #902)			
Title services and lender's title insurance (HUD-1/1A Line #1101)	$975.00	$975.00	
Optional owner's title insurance (HUD-1/1A Line #1110)	$679.00	$725.00	
____ (HUD-1/1A Line #____)			
Total	**$2052.00**	**$2136.00**	**+84**
***Increase between GFE and HUD-1/1A Charges**	**4%**		
Charges Can Change			
Reserves or escrow (HUD-1/1A Line #1001)	$262.00	$262.00	
Daily interest charges (HUD-1/1A Line #901) $53.42 per day	$213.69	$427.36	
Homeowners insurance (HUD-1/1A Line #903)	$600.00	$615.00	
Survey (HUD-1/1A Line #1301)	$150.00	$150.00	
Pest inspection (HUD-1/1A Line #1302)	$35.00	$35.00	
____ (HUD-1/1A Line #____)			

Acknowledgment

The undersigned hereby state that the Closing Script was read and the following information was provided and explained:

1. The comparison between the charges listed on the HUD-1/1A settlement form and the estimate of charges on the GFE;
2. Whether or not the tolerances have been met within the applicable categories between the GFE and the HUD-1/1A; and
3. Any inconsistencies between the loan documents (including the mortgage note) and the summary of the loan terms on the GFE, and between the HUD-1/1A settlement charges and the charges stated on the GFE.

___________________ (Representative) ___________________ (Company)

___________________ (Borrower) ___________________(Borrower)

___________________ (Date)

Example 5 – Fixed Interest Rate with Balloon Payment

THESE ARE YOUR LOAN DETAILS

The following is a summary of many important details involving the mortgage loan for 123 Main Street, Hometown, USA 00000. Let's compare these important details with the Good Faith Estimate (GFE), loan documents, and other disclosures.

Loan Amount	Loan Term	Loan Type
$300,000.00	**15 year**	**Conventional Fixed Rate Interest Only Balloon**

Fixed Interest Rate

Your loan has a fixed interest rate of **7.5%**.

A fixed interest rate means that your interest rate will not rise over the life of the loan.

Payment - Interest-Only Mortgage

Your loan payment for interest (**$1,875.00**) and mortgage insurance (**$62.00**) is **$1,937.00** and **cannot rise**. This will not reduce the principal balance of your loan.

You have an escrow account. In addition to any mortgage insurance, your initial escrow payment is **$200.00** for property taxes and homeowners insurance. This amount may increase.

Your total payment is **$2,137.00** for interest, any mortgage insurance, property taxes and homeowners insurance.

Late Payment

Your loan payment is due on the 1st of every month and is considered late after the 15th of every month. If your lender receives your mortgage payment after the 15th, your lender will charge a late fee of **5%** of the overdue payment of principal and interest.

Loan Balance

Your loan balance **cannot** rise.

Prepayment Penalty

You **have** a pre-payment penalty.

A prepayment penalty is an additional amount that you will be required to pay if you pay your loan off early such as through the sale of your home, refinancing your loan, or if you make significant additional payments to principal prior to **June 1, 2010**. Based on your initial loan amount, your prepayment penalty may be as high as **$9,400.00**.

Balloon Loan

Your loan has a balloon payment. At the end of the loan term, any balance remaining will have to be paid. In the case of a balloon loan, often very little, if any, of the loan balance is paid down, therefore, the last payment, the balloon payment can be most of the initial loan balance. Most consumers with a balloon note refinance their loan before the final balloon payment becomes due.

Your balloon payment will become due on **April 1, 2023** in the amount of **$300,000.00**.

Closing Costs

Next we will review all of the HUD-1/1A charges and credits associated with your loan and compare them to the GFE you received when you applied for this loan.

GFE & HUD-1/1A Charges Comparison Chart

	Good Faith Estimate	HUD-1/1A	$ Increase
Charges Cannot Increase			
Our service charge (HUD-1/1A Line #801)	$6,000.00	$6,000.00	0
Your credit or charge for the specific interest rate chosen (HUD-1/1A Line #802)	-$4,000.00	-$4,000.00	0
Your Adjusted Origination Charges (HUD-1/1A Line #803)	$2,000.00	$2,000.00	0
Government recording and transfer charges (HUD-1/1A Line #1201)	$1,250.00	$1,250.00	0
Charges Cannot Increase More Than 10%			
Appraisal (HUD-1/1A Line #804)	$300.00	$300.00	
Credit Report (HUD-1/1A Line #805)	$40.00	$45.00	
Tax service (HUD-1/1A Line #806)	$70.00	$92.00	
Flood certification (HUD-1/1A Line #807)	$12.00	$15.00	
Mortgage Insurance Premium (HUD-1/1A Line #902)	$62.00	$62.00	
Title services and lender's title insurance (HUD-1/1A Line #1101)	$975.00	$1015.00	
Optional owner's title insurance (HUD-1/1A Line #1110)	$725.00	$775.00	
______ (HUD-1/1A Line #____)			
Total	**$2184.00**	**$2304.00**	**+120**
***Increase between GFE and HUD-1/1A Charges**	**5%**		
Charges Can Change			
Reserves or escrow (HUD-1/1A Line #1001)	$262.00	$262.00	
Daily interest charges (HUD-1/1A Line #901) $53.42 per day	$213.69	$427.36	
Homeowners insurance (HUD-1/1A Line #903)	$600.00	$600.00	
Survey (HUD-1/1A Line #1301)	$175.00	$175.00	
Pest Inspection (HUD-1/1A Line #1302)	$45.00	$45.00	
______ (HUD-1/1A Line #____)			

Acknowledgment

The undersigned hereby state that the Closing Script was read and the following information was provided and explained:

1. The comparison between the charges listed on the HUD-1/1A settlement form and the estimate of charges on the GFE;

2. Whether or not the tolerances have been met within the applicable categories between the GFE and the HUD-1/1A; and
3. Any inconsistencies between the loan documents (including the mortgage note) and the summary of the loan terms on the GFE, and between the HUD-1/1A settlement charges and the charges stated on the GFE.

__________________ (Representative) __________________ (Company)

__________________ (Borrower) __________________(Borrower)

__________________ (Date)

Example 6 –Fixed Interest Rate with Balloon Payment

THESE ARE YOUR LOAN DETAILS

The following is a summary of many important details involving the mortgage loan for 123 Main Street, Hometown, USA 00000. Let's compare these important details with the Good Faith Estimate (GFE), loan documents, and other disclosures.

Loan Amount	Loan Term	Loan Type
$30,000.00	15 year	Conventional Fixed Rate Balloon

Fixed Interest Rate

Your loan has a fixed interest rate of **8.0%**.

A fixed interest rate means that your interest rate will not rise over the life of the loan.

Payment

Your loan payment for principal and interest (**$220.13**) and mortgage insurance (**$0**) is **$220.13** and **cannot** rise.

You do not have an escrow account. Any and all items such as property taxes and homeowners insurance must be paid directly by you.

Your total payment is **$220.13** for principal, interest, and any mortgage insurance.

Late Payment

Your loan payment is due on the 1st of every month and is considered late after the 15th of every month. If your lender receives your mortgage payment after the 15th, your lender will charge a late fee of **5%** of the overdue payment of principal and interest.

Loan Balance

Your loan balance **cannot** rise.

Prepayment Penalty

You **have** a pre-payment penalty.

A prepayment penalty is an additional amount that you will be required to pay if you pay your loan off early such as through the sale of your home, refinancing your loan, or if you make significant additional payments to principal prior to **June 1, 2010**. Based on your initial loan amount, your prepayment penalty may be as high as **$9,400.00**.

Balloon Loan

Your loan has a balloon payment. At the end of the loan term, any balance remaining will have to be paid. In the case of a balloon loan, often very little, if any, of the loan balance is paid down, therefore, the last payment, the balloon payment can be most of the initial loan balance. Most consumers with a balloon note refinance their loan before the final balloon payment becomes due.

Your balloon payment will become due on **April 1, 2023** in the amount of **$300,000.00**.

Closing Costs

Next we will review all of the HUD-1/1A charges and credits associated with your loan and compare them to the GFE you received when you applied for this loan.

GFE & HUD-1/1A Charges Comparison Chart

	Good Faith Estimate	HUD-1/1A	$ Increase
Charges Cannot Increase			
Our service charge (HUD-1/1A Line #801)	$2,700.00	$2,700.00	0
Your credit or charge for the specific interest rate chosen (HUD-1/1A Line #802)	-$750.00	-$750.00	0
Your Adjusted Origination Charges (HUD-1/1A Line #803)	$1,950.00	$1,950.00	0
Government recording and transfer charges (HUD-1/1A Line #1201)	$1,250.00	$1,250.00	0
Charges Cannot Increase More Than 10%			
Appraisal (HUD-1/1A Line #804)	$300.00	$325.00	
Credit Report (HUD-1/1A Line #805)	$22.00	$18.00	
Tax service (HUD-1/1A Line #806)	$60.00	$78.00	
Flood certification (HUD-1/1A Line #807)	$12.00	$15.00	
Mortgage Insurance Premium (HUD-1/1A Line #902)			
Title services and lender's title insurance (HUD-1/1A Line #1101)	$415.00	$469.00	
______ (HUD-1/1A Line #____)			
______ (HUD-1/1A Line #____)			
Total	**$809.00**	**$905.00**	**+96**
***Increase between GFE and HUD-1/1A Charges**	**12%**		
Charges Can Change			
Reserves or escrow (HUD-1/1A Line #1001)			
Daily interest charges (HUD-1/1A Line #901) $7.24 per day	$28.96	$57.92	
Homeowners insurance (HUD-1/1A Line #903)	$600.00	$600.00	
______ (HUD-1/1A Line #____)			
______ (HUD-1/1A Line #____)			
______ (HUD-1/1A Line #____)			

Acknowledgment

The undersigned hereby state that the Closing Script was read and the following information was provided and explained:

1. The comparison between the charges listed on the HUD-1/1A settlement form and the estimate of charges on the GFE;
2. Whether or not the tolerances have been met within the applicable categories between the GFE and the HUD-1/1A; and
3. Any inconsistencies between the loan documents (including the mortgage note) and the summary of the loan terms on the GFE, and between the HUD-1/1A settlement charges and the charges stated on the GFE.

__________________ (Representative) __________________ (Company)

__________________ (Borrower) __________________(Borrower)

__________________ (Date)

BILLING CODE 4210–67–C

15. Appendix C to part 3500 is revised to read as follows:

APPENDIX C TO PART 3500—INSTRUCTIONS FOR COMPLETING GOOD FAITH ESTIMATE (GFE) FORM

The following are instructions for completing the GFE required under section 5 of RESPA and 24 CFR 3500.7 (Regulation X) of the Department of Housing and Urban Development regulations. The standardized form set forth in this Appendix is the required GFE form and must be provided exactly as specified. The instructions for completion of the GFE are primarily for the benefit of the loan originator who prepares the form and need not be transmitted to the borrower(s) as an integral part of the GFE. The required, standardized GFE form must be prepared completely and accurately. A separate GFE must be provided for each loan where a transaction will involve more than one mortgage loan.

General instructions

The loan originator preparing the GFE may fill in information and amounts on the form by typewriter, hand printing, computer printing, or any other method producing clear and legible results. Under these instructions, the ''form'' refers to the required, standardized GFE form. Although the standardized, required GFE is a prescribed form, sections 3 and 5 on page 2 may be adapted for use in particular loan situations, similarly to the way the Form HUD–1 Settlement Statement is adaptable, so that if additional lines are needed in those blocks on the GFE, additional lines may be inserted there.

All fees for categories of charges shall be disclosed in U.S. dollar amounts.

Specific instructions

Page 1.

Top of the Form—The loan originator must enter its name, business address, telephone number and email address on the top of the form, along with the borrower's (GFE applicant's) name, the address of the property for which financing is sought, and the date of the GFE.

''Instructions''—This section requires no loan originator action.

''Important dates.''—This section briefly states important deadlines that the GFE applicant must meet during the GFE application and mortgage application processes in order to obtain the loan product that is the subject of the GFE. In Line 1, the loan originator must state the date until which the interest rate for the GFE will be available. In Line 2, the loan originator must state the date until which the estimate of all other settlement charges for the GFE will be available. In Line 3, the loan originator must state how many days within which time the GFE applicant has to go to settlement from the start of the mortgage application process, and how many days prior to settlement the interest rate would have to be locked.

''Summary of Your Loan Terms''—In the section entitled ''Your Loan Details'', for all loans, the loan originator must fill in:

(i) The initial loan balance;

(ii) The loan term;

(iii) The initial interest rate; and

(iv) The initial monthly amount owed for principal, interest and any mortgage insurance.

The loan originator must also specify the rate lock period in days informing the borrower that after the borrower locks in his or her interest rate, the borrower must go to settlement within this period to receive that interest rate.

The loan originator must indicate whether the interest rate can rise, and, if so, insert the maximum rate to which it can rise. The loan originator must indicate whether the loan balance can rise, and, if so, insert the maximum amount to which it can rise. (If the loan balance will increase only because escrow is run out of the loan balance, the loan originator is not required to check the box indicating that the loan balance can rise.) The loan originator must indicate whether the monthly amount owed for principal, interest, and any mortgage insurance might rise, and, if so, insert the maximum amount to which it can rise. The loan originator must indicate whether the loan includes a prepayment penalty, and, if so, the maximum amount that it could be. The loan originator must indicate whether the loan requires a balloon payment and, if so, the maximum amount, and in how many years it will be due. The loan originator must also indicate whether the loan includes a monthly escrow payment for property taxes and other financial obligations.

''*Summary of your settlement charges*''—In this section, the loan originator must state its own charges (''Your Adjusted Origination Charge'') based on the calculation of Blocks 1 and 2 on page 2, as entered at highlighted Line A on page 2. The loan originator must provide the total charge for all other services (''Your Charges for All Other Settlement Services'') based on the addition of the sums in Blocks 3 through 10 on page 2, as entered at highlighted Line B on page 2. The loan originator must provide the sum of these two numbers (''Total Estimated Settlement Charges''), as entered at highlighted Line A+B on page 2.

Page 2.

''*Understanding Your Estimated Settlement Charges*''—This section details the ten settlement cost categories and amounts associated with the mortgage loan. For purposes of determining whether the tolerance has been met, the amount on the GFE should be compared with the total of any amounts shown on the HUD–1 in the borrower's column and any amounts shown as ''P.O.C. (borrower).''

''Your Loan Details''

Block 1, ''*Our service charge*''—The loan originator must state here all charges that all loan originators involved in this transaction will receive, except for any charges for the interest rate chosen noted in Block 2. The amount stated in Block 1 is subject to zero tolerance, i.e., the amount may not increase at settlement.

Block 2, ''*Your credit or charge for the specific interest rate chosen (points)*''—The loan originator must indicate through check boxes whether there is a credit to the borrower for the interest rate chosen on the loan, and the amount of the credit, or whether there is an additional up-front charge to the borrower for the interest rate chosen on the loan, and the amount of that charge. A credit and charge cannot occur together in the same transaction. A lender may choose not to separately disclose any credit or charge for the interest rate chosen on the loan in this block; however, if this block does not include any positive or negative figure, the lender must check the first box to indicate that ''The credit or charge for the interest rate you have chosen'' is included in ''Our service charge'' above. (See Block 1 instructions above.) For a mortgage broker, the credit or charge for the specific interest rate chosen is the difference between the initial loan amount and the payment to the mortgage broker (i.e., the sum of the price paid for the loan by the lender and any other payments to the mortgage broker from the lender). When the amount paid to the mortgage broker exceeds the initial loan amount, there is a credit to the borrower and it is entered as a negative amount in Block 2 of the GFE. When the initial loan amount exceeds the amount paid to the mortgage broker, there is a charge to the borrower and it is entered as a positive amount in Block 2 of the GFE. The amount stated in Block 2 is subject to zero tolerance while the interest rate is locked, i.e., any charge for the interest rate chosen cannot increase and any credit for the interest rate chosen cannot decrease in absolute value terms.

Line A, ''*Your Adjusted Origination Charges*''—The loan originator must add the numbers in Blocks 1 and 2 and enter this subtotal at highlighted Line A. The subtotal at Line A will be a negative number if there is a credit in Block 2 that exceeds the charge in Block 1. The amount stated in Line A is subject to zero tolerance while the interest rate is locked.

In the case of ''no cost'' loans where ''no cost'' refers only to the loan originator's fees, Line A must show a zero charge as the adjusted origination charge. In the case of ''no cost'' loans where ''no cost'' encompasses third party fees as well as the up-front payment to the loan originator, the third party fees listed in Block 3 through Block 10, to be paid for by the loan originator, must be itemized and listed on the GFE, and the total for Line A will result in a negative number equal to the third party fees covered in the loan originator's definition of ''no cost.''

''Your Charges for All Other Settlement Services''

Block 3, ''*Required services that we select*''—In this block, the loan originator must identify each third party settlement service required and selected by the loan originator (excluding title services), along with the estimated price to be paid to the provider of each service. The loan originator must identify the specific required services and provide an estimate of the price of each service. Loan originators are also required to add the individual prices disclosed in this block and place the total in the right-hand column of this block. Where a loan originator permits a borrower to shop for third party settlement services, the loan originator must provide the borrower with a written list of settlement services providers at the time of the GFE, on a separate sheet of paper. The 10 percent tolerance applies to the sum of the prices of each service listed in Block 3, Block 4, Block 5, and Block 10, where the loan originator requires the use of a particular provider or the borrower uses a provider selected or identified by the loan originator. Any services in Block 4, Block 5, or Block 10 for which the borrower selects a provider other than one identified by the loan originator are not subject to any tolerance and should not be included in the sum of the prices on which the 10 percent tolerance is based.

Block 4, ''*Title services and lender's title insurance*''—In this block, the loan originator must state the estimated total price paid to third party settlement service providers for all title related services and lender's title insurance premiums, when such services are required by the loan originator, regardless of whether they are selected by the prospective borrower or the loan originator. Where a loan originator permits a borrower to shop for title services and lender's title insurance, the loan originator must provide the borrower with a written list of title services providers at the time of the GFE on a separate sheet of paper. The price shown in this block is subject to an overall 10 percent tolerance as described in the instructions for Block 3 above, if the borrower selects one of the title services providers identified by the loan originator.

Block 5, ''*Required services that you can shop for*''—In this block, the loan originator must identify each third party settlement service required by the loan originator where the borrower is permitted to shop for and select the settlement service provider (excluding title services), along with the estimated price to be paid to the provider of each service. The loan originator must identify the specific required services and provide an estimate of the price of each service. The loan originator must also add the individual prices disclosed in this block and place the total in the right-hand column of this block. Where a loan originator permits a borrower to shop for a required settlement service, the loan originator must provide the borrower with a written list of settlement service providers at the time of the GFE, on a separate sheet of paper. The prices shown in this block are subject to an overall 10 percent tolerance as described in the instructions for Block 3 above, if the borrower selects a settlement service provider identified by the loan originator.

Block 6, ''*Government Recording and Transfer Charges*''—Based upon the proposed loan amount and/or sales price, and the property address, a loan originator must estimate in this block the sum of all state and local government fees, charges, and taxes, usually resulting from the mortgage loan or property transfer, which can be expected to be charged at settlement. A zero tolerance applies to the sum of these estimated fees.

Block 7, ''*Reserves or escrow*''—In this block, the loan originator must estimate the amount that the borrower will be required to place in a reserve or escrow account at settlement to be applied to periodic property tax, homeowner's insurance, mortgage insurance payments, or other periodic charges.

Block 8, ''*Daily interest charges*''—In this block, the loan originator must enter the daily interest amount applicable to the proposed loan and estimate the total amount that will be due at settlement, based on a closing date that the loan originator is to identify in this block, and list the specific number of days.

Block 9, ''*Homeowner's insurance*''—The loan originator must estimate in this block the premium amount for a hazard insurance policy meeting the loan originator's requirements. To the extent a loan originator requires that hazard insurance be part of the escrow account, the amount of the initial escrow deposit must be properly included in Block 7.

Block 10, ''*Optional owner's title insurance*''—In this block, the loan originator must estimate the price of an owner's title insurance policy. The loan originator must provide the borrower with a written list of providers of owner's title insurance at the time of the GFE on a separate sheet of paper. The price shown in this block is subject to an overall 10 percent tolerance as described in the instructions for Block 3 above, if the borrower selects a title services provider identified by the loan originator.

Line B, ''*Your Charges for All Other Settlement Services*''—The loan originator shall add the numbers in Blocks 3 to10 and enter this subtotal at highlighted Line B.

Line A + B, ''*Total Estimated Settlement Charges*''—The loan originator shall add the numbers at highlighted Lines A and B and enter the total at highlighted Line A + B.

Page 3.

''Important Information and Instructions''

''Shopping for a loan offer''—The section requires no loan originator action.

''*Understanding Which Charges Can Change at Settlement*''—This section informs the prospective borrower of which categories of settlement charges can increase at closing, and by how much, and which categories of settlement charges cannot increase at closing. This section requires no loan originator action.

''*Looking at Trade-offs*''—This section is designed to make borrowers aware of the relationship between their total estimated settlement charges on one hand, and the proposed interest rates and resulting monthly payments on the other hand. The loan originator must complete the left hand column using the loan amount, interest rate, monthly payment figure, and the total estimated settlement charges from page 1. The loan originator must provide the borrower with the same information for two alternative loans, one with a higher interest rate, if available, and one with a lower interest rate, if available, from the loan originator. The alternative loans must use the same loan amount and be otherwise identical to the loan in the GFE. The loan originator must fill in the trade-off chart to show the borrower the loan amount, alternative interest rate, alternative monthly payment, the change in the monthly payment from the loan in this GFE to the alternative loan, the change in the total settlement charges from the loan in this GFE to the alternative loan, and the total settlement charges for the alternative loan. If either of the alternative loans are not available from the loan originator, the loan originator should so indicate with N. A. (i.e., Not Available), in the appropriate column(s). If these options are available, an applicant may request a new GFE, and a new GFE must be provided by the loan originator.

Page 4.

''*Your financial responsibilities as a homeowner*''—In this section, the loan originator must enter the estimated annual amount for property taxes, and any homeowner's, flood, or other required property protection insurance that the GFE applicant may incur in order to retain the mortgaged property. The remainder of this section requires no loan originator action.

''*Applying for this loan*''—In this section, the loan originator must provide its contact information, i.e., name and telephone number or email address, and specify any fee the borrower must pay to proceed with the mortgage application.

''Getting More Information''—The section requires no loan originator action.

''*Using the shopping chart*''—This chart is a shopping tool to be provided by the loan originator for the borrower to complete to compare GFEs.

''*If your loan is sold in the future*''—This section requires no loan originator action.

BILLING CODE 4210–67–P

OMB No. xxxx-xxxx
Approval Expires mm/dd/yyyy

Good Faith Estimate (GFE)

Name of Originator
Borrower
Originator Address
Property Address
Originator Phone Number
Originator email
Date of GFE

Instructions

This GFE gives you an estimate of your settlement charges and loan terms if you are approved for this loan. See page 3 for more detailed instructions.

Important dates

1. The interest rate for this GFE is available until . After that date, the interest rate, some of your Loan Origination Charges, and the monthly payment shown below can change until you lock your interest rate.
2. This estimate for all other settlement charges is available until
3. If you proceed with this loan, you must go to settlement in days. You must lock the interest rate at least days before settlement.

Summary of your loan terms

Your Loan Details		
Your initial loan balance is	$	
Your loan term is	years	
Your initial interest rate is	%	
Your initial monthly amount owed for principal, interest, and any mortgage insurance is	$ per month	
Your rate lock period is *After you lock in your interest rate, you must go to settlement within this number of days to guarantee this interest rate.*	days	
Can your interest rate rise?	☐ No	☐ Yes, it can rise to a maximum of %
Can your loan balance rise?	☐ No	☐ Yes, it can rise to a maximum of $
Can your monthly amount owed for principal, interest, and any mortgage insurance rise?	☐ No	☐ Yes, it can rise to a maximum of $
Does your loan have a prepayment penalty?	☐ No	☐ Yes, your maximum prepayment penalty is $
Does your loan have a balloon payment?	☐ No	☐ Yes, you have a balloon payment of $ due in years.
Does your loan include a monthly escrow payment for property taxes and, possibly, other obligations?	☐ No	☐ Yes

Summary of your settlement charges

A	Your Adjusted Origination Charges *(Table A, page 2)*	$
B	Your Charges for All Other Settlement Services *(Table B, page 2)*	$
A+B	Total Estimated Settlement Charges	$

This form is also on www.hud.gov/respa

Understanding your estimated settlement charges

Your Loan Details

1. Our service charge
These charges are for the services we provide when we get and process this loan for you.

2. Your credit or charge for the specific interest rate chosen (points)
- ☐ The credit or charge for the interest rate you have chosen is included in "Our service charge." (See item 1 above.)
- ☐ You receive a credit of $ for this interest rate of %. This credit reduces your upfront charges.
- ☐ You pay a charge of $ for this interest rate of %. This payment (discount points) increases your upfront charges. (See the table on page 3 to see how you can change this charge or credit by choosing a different interest rate.)

A Your Adjusted Origination Charges $

Your Charges for All Other Settlement Services

3. **Required services that we select**
These charges are for services we require to complete your settlement. We will choose the providers of these services.

Service	*Charge*

4. **Title services and lender's title insurance**
This charge includes the services of a title agent, for example, and title insurance to protect the lender, if required.

5. **Required services that you can shop for**
These charges are for other services that are required to complete your settlement. We can refer you to providers of these services or you can shop for them yourself. Our estimates for providing these services are below.

Service	*Charge*

6. **Government recording and transfer charges**
This includes state and local charges on mortgages and home sales.

7. **Reserves or escrow**
This charge is held in an escrow account to pay recurring charges on your property, such as property taxes or insurance.

8. **Daily interest charges**
This charge is for the daily interest on your loan from the day of your settlement until the first day of the next month or the first day of your normal mortgage payment cycle. For this loan, this amount is $ per day for days (if your closing date is).

9. **Homeowner's insurance**
This charge is for the insurance you must buy for the property to protect from a loss, such as fire.

10. **Optional owner's title insurance**
This charge is for additional insurance you can choose to buy to protect yourself from title defects.

B Your Charges for All Other Settlement Services $

A + B Total Estimated Settlement Charges $

Important Information and Instructions

Shopping for a loan offer

Only you can shop for the best loan for you. Compare this GFE with other loan offers, so you can find the best loan. Use the table on page 4 to compare all the offers you receive.

Understanding which charges can change at settlement

The GFE estimates your settlement charges. At your settlement, you will receive a HUD-1. Compare the charges on the HUD-1 with the charges on this GFE. Charges can change if you select your own provider and do not use the companies your lender suggests.

The list below shows you how much the estimated charges on this GFE can change at your closing.

These charges ***cannot increase*** at settlement:	The total of these charges *can increase up to 10%* at settlement:	These charges ***can change*** at settlement:
• Our service charge • Your charge or credit for the specific interest rate chosen *(after you lock in your interest rate)* • Government recording and transfer charges	• Required services that we select • Title services and lender's title insurance *(if we select them or you use providers identified by us)* • Required services that you can shop for *(if you use providers identified by us)* • Optional owner's title insurance *(if you use providers identified by us)*	• Required services that you can shop for *(if you do not use providers identified by us)* • Title services and lender's title insurance *(if you do not use providers identified by us)* • Reserves or escrow • Daily interest rate charges • Homeowner's insurance • Optional owner's title insurance *(if you do not use providers identified by us)*

Looking at trade-offs

In this GFE, we offered you a particular interest rate and estimated settlement charges. But, you could choose other loans to get a lower interest rate or lower settlement charges.

■ If you want to choose a loan with a **lower interest rate,** then you will have **higher settlement charges.**

■ If you want to choose a loan with **lower settlement charges,** then you will have a **higher interest rate.**

The table below shows how the loan for this GFE compares to two other options. If you decide you want to make one of these trade-offs, you must ask us for a new GFE.

	The loan in this GFE	A loan with a lower interest rate	A loan with lower settlement charges
Your loan amount	$	$	$
Your interest rate	%	%	%
How much your monthly payment will be	$	$	$
How much more or less in monthly payments from this GFE	No Change	You will pay $ less every month	You will pay $ more every month
How much more or less you will pay at settlement with this interest rate	No Change	Your lower interest rate will raise your settlement charges by $	Your higher interest rate will lower your settlement charges by $
How much your total estimated settlement charges will be	$	$	$

If this loan offer is for an adjustable rate loan, the comparisons in the table are for the initial interest rate before any adjustments are made.

Your financial responsibilities as a homeowner

In addition to your monthly amount owed for principal, interest, and mortgage insurance, you may need to pay other required annual charges to keep your property. We must provide an estimate for annual property taxes along with homeowner's, flood, and other required property protection insurance, but we are not required to provide estimates for the other charges. You may have to identify the other charges and ask for additional estimates from others.

Different sources might use different techniques to estimate these charges, but the actual charges will be the same in the end. Therefore, do not use these estimates to compare settlement charges from different loan originators.

Annual property taxes ....

Annual homeowner's insurance ....

Annual flood insurance ....

Annual homeowners association/condominium fees. . . .

Other ....

Total Other Annual Charges ....

Applying for this loan

If you decide you would like to apply for this loan, contact us at
You must pay a fee of $ This fee will be subtracted from your settlement charges.

Getting more information

The type of loan you choose can affect your current and future monthly payments. You can ask us for more information about loan types. You can also look at several government publications: HUD's *Special Information Booklet* on settlement charges, your *Truth-in-Lending Disclosures*, and consumer information publications of the Federal Reserve Board.

Using the shopping chart

Use this chart to compare Good Faith Estimates (GFEs) from different loan originators. Fill in the information by using a different column for each GFE you receive.

By comparing loan offers, you can shop for the best loan.

	Loan 1	Loan 2	Loan 3	Loan 4
Loan Originator Name				
Initial Loan Balance				
Loan Term				
Initial Interest Rate				
Initial Monthly Amount Owed				
Rate Lock Period				
Can Interest Rate Rise?				
Can Loan Balance Rise?				
Can Monthly Amount Owed Rise?				
Prepayment Penalty?				
Balloon Payment?				
Total Estimated Settlement Charges				

If your loan is sold in the future

Lenders can receive additional fees by selling your loan at some future date after settlement. Once you have obtained your loan at settlement, however, your loan terms, adjusted origination charges, and total settlement charges cannot change. After settlement, any fees lenders receive in the future cannot change the loan you received or the charges you paid at settlement.

BILLING CODE 4310–67–C

16. Appendix E to part 3500 is amended by removing the parenthetical "(Existing Accounts)" from the heading,

''II. Example Illustrating Single-Item Analysis (Existing Accounts)''.

17. Appendix MS–1 to part 3500 is revised to read as follows:

APPENDIX MS–1 TO PART 3500

[Sample language; use business stationery or similar heading]

[Date]

SERVICING DISCLOSURE STATEMENT

NOTICE TO FIRST LIEN MORTGAGE LOAN APPLICANTS: THE RIGHT TO COLLECT YOUR MORTGAGE LOAN PAYMENTS MAY BE TRANSFERRED

You are applying for a mortgage loan covered by the Real Estate Settlement Procedures Act (RESPA) (12 U.S.C. 2601 *et seq.*). RESPA gives you certain rights under Federal law. This statement describes whether the servicing for this loan may be transferred to a different loan servicer. ''Servicing'' refers to collecting your principal, interest, and escrow payments, if any. You will be given advance notice before a transfer occurs.

Servicing Transfer Information

[We may assign, sell, or transfer the servicing of your loan while the loan is outstanding.]

[or]

[We do not service mortgage loans of the type for which you applied. We intend to assign, sell, or transfer the servicing of your mortgage loan before the first payment is due.]

[or]

[The loan for which you have applied will be serviced at this financial institution and we do not intend to sell, transfer, or assign the servicing of the loan.]

[INSTRUCTIONS TO PREPARER: Insert the date and select the appropriate language under ''Servicing Transfer Information.'' The model format may be annotated with further information that clarifies or enhances the model language.]

Dated: February 8, 2008.

Brian D. Montgomery,

Assistant Secretary for Housing—Federal Housing Commissioner.

Note: The following appendix will not appear in the Code of Federal Regulations.

Appendix to FR–5180 Proposed Rule on Regulatory Flexibility Analysis

The following Regulatory Flexibility Analysis is Chapter 6 of the rule's Economic Analysis, which is available for public inspection and available online at *www.hud.gov/respa.*

Appendix I. Introduction to the Rule's Benefits and Impacts on Small Businesses

This appendix is the Initial Regulatory Flexibility Analysis (IRFA) of the proposed rule as described under Section 604 of the Regulatory Flexibility Act. The requirements of the IRFA are listed below along with references to where the requirements are covered in the IRFA and where more detailed discussion can be found in other chapters of the Regulatory Impact Analysis (RIA).

(1) *A description of the reasons why action by the agency is being considered* can be found in Section III of this appendix, in Section II of Chapter 1 of the Regulatory Impact Analysis (RIA), and in greater detail in the first sections of Chapters 3 and 4 of the RIA.

(2) *A succinct statement of the objectives of, and legal basis for, the proposed rule is* provided in Section III of this appendix. This is also discussed in Section II of Chapter 1 of the Regulatory Impact Analysis and in greater detail in the first sections of Chapters 3 and 4 of the RIA.

(3) *A description and an estimate of the number of small entities to which the rule will apply or an explanation of why no such estimate is available.* Section V of this Appendix provides data on small businesses that may be affected by the rule. As explained in Section V, Chapter 5 of the Regulatory Impact Analysis also provides extensive documentation of the characteristics of the industries directly affected by the rule, including various estimates of the numbers of small entities, reasons why various data elements are not reliable or unavailable, and descriptions of methodologies used to estimate (if possible) necessary data elements that were not readily available. The industries discussed in Chapter 5 of the RIA included the following (with section reference): mortgage brokers (Section II); lenders including commercial banks, thrifts, mortgage banks, credit unions (Section III); settlement and title services including direct title insurance carriers, title agents, escrow firms, and lawyers (Section IV); and other third-party settlement providers including appraisers, surveyors, pest inspectors, and credit bureaus (Section V); and real estate agents (Section VI). As explained in Section V of this chapter, Appendix A includes estimates of revenue impacts for the new Good Faith Estimate (GFE).

(4) *A description of the projected reporting, record keeping, and other compliance requirements of the rule, including an estimate of the classes of small entities that will be subject to the requirement and the types of professional skills necessary for preparation of the report or record.* Compliance requirements and costs are discussed in Sections VII through IX of this appendix. In no case are any professional skills required for reporting, record keeping, and other compliance requirements of this rule that are not otherwise required in the ordinary course of business of firms affected by the rule. As noted above, Chapter 5 of the RIA includes estimates of the small entities that may be affected by the rule.

(5) *An identification, to the extent practicable, of all relevant Federal rules which may duplicate, overlap or conflict with the proposed rule.* The proposed rule provisions for describing loan terms in the new GFE and the HUD–1 closing script are somewhat duplicative of the Truth in Lending Act (TILA) regulations; however the differences in approach between the TILA regulations and HUD's proposed RESPA rule make the duplication less than complete. Overlaps are discussed further in this chapter.

In addition, this appendix contains (c) *a description of any significant alternatives to the proposed rule which accomplish the stated objectives of applicable statutes and which minimize any significant impact of the proposed rule on small entities.* The IRFA also describes comments dealing with compliance and regulatory burden in the 2002 proposed rule. Some of the comments were on provisions of the 2002 proposed rule that have been dropped. Other comments were on impacts that the Department believes will be small or non-existent. Some of the compliance and regulatory burden comments concerned costs that are only felt during the start-up period and are one-time costs. These are discussed in Section VII.B of the Appendix, while comments on recurring costs of implementing the new GFE form are addressed in Section VII.C. Section VII.D pf the Appendix discusses GFE-related changes in the proposed rule that reduce regulatory burden. Section VII.E discusses compliance issues related to GFE tolerances on settlement party costs, while Section VII.F discusses efficiencies associated with the new GFE.

Before proceeding further, Section II provides a brief summary of the main findings from the Regulatory Impact Analysis that relate to the proposed rule. The summary is provided for those readers who do not have ready access to the other chapters of the Regulatory Impact Analysis. Some readers may want more details on the anticipated competitive and market effects of the new GFE on small businesses. These are discussed in Chapter 3 of the RIA in Sections VIII.A (mortgage brokers), VIII.B (lenders), VIII.C (title and settlement third-party firms), and VIII.D (other third-party firms).

Appendix II. Summary of the Regulatory Impact Analysis

This summary follows the same outline as the Executive Summary of the RIA: beginning with an overview of the proposed rule; a discussion of the problems with the mortgage shopping process and the current GFE; followed by a description of the main components of the changes to the GFE; and a review of the anticipated benefits and market effects of the proposed rule.

Appendix III. Overview of Proposed Rule

HUD has issued a proposed rule under the Real Estate Settlement Procedures Act (RESPA) to simplify and improve the process of obtaining home mortgages and to reduce settlement costs for consumers. This Regulatory Impact Analysis and Regulatory Flexibility Analysis examine the economic effects of that rule.[35] As this Regulatory Impact Analysis demonstrates, the proposed rule is expected to improve consumer shopping for mortgages and to reduce the costs of closing a mortgage transaction for the consumer. Consumer savings were estimated under a variety of scenarios about originator and settlement costs. In the base case, the estimated price reduction to borrowers comes to $8.35 billion or $668 per loan. This

[35] The term ''Economic Analysis'' will often be used to refer to both the Regulatory Flexibility Analysis as well as the Regulatory Impact Analysis.

represents the substantial savings that can be achieved with the proposed rule.

The proposed RESPA rule includes a new, simplified Good Faith Estimate (GFE) that includes tolerances on final settlement costs and a new method for reporting wholesale lender payments in broker transactions. The proposed rule allows settlement service providers to seek discounts, including volume based discounts, for settlement services, which should lead to lower third-party settlement service prices. In addition, the proposed rule allows service providers to use average cost pricing for third-party services they purchase, making their business operations simpler and less costly. Competition among loan originators will put pressure for these cost savings to be passed on to borrowers. The proposed GFE will produce substantial shopping and price-reduction benefits for both origination and third-party settlement services.

To increase the value of the new GFE as a shopping document, HUD is proposing revisions to the HUD–1 Settlement Statement form that will make the GFE and HUD–1 easier to compare. The revised HUD–1 uses the same language to describe categories of charges as the GFE, and orders the categories of charges in the same way. This makes it much simpler to compare the two documents and confirm whether the tolerances required in the new GFE have been met or exceeded. In addition, the proposed rule requires as an addendum to the revised HUD–1, the preparation and reading of a closing script that would: (1) Compare the GFE to the HUD–1 and advise borrowers whether tolerances have been met or exceeded; (2) verify that the loan terms summarized on the GFE match those in the loan documents, including the mortgage note; and (3) provide additional information on the terms and conditions of the mortgage. All three of these components of the rule, together, are required fully to realize the consumer saving on mortgage closing cost estimated here.

Given that there has been no significant change in the basic HUD–1 structure and layout, generating this new HUD–1 should not pose any problem for firms closing loans—in fact, the closing process will be much simpler given that borrowers and closing agents can precisely link the information on the initial GFE to the information on the final HUD–1.

Because the proposed rule calls for significant changes in the process of originating a mortgage, this Regulatory Impact Analysis identifies a wide range of benefits, costs, efficiencies, transfers, and market impacts. The effects on consumers from improved borrower shopping will be substantial under this rule. Similarly, the use of tolerances will place needed controls on origination and third-party fees. Ensuring that yield spread premiums are credited to borrowers in brokered transactions could cause significant transfers to consumers. The increased competition associated with RESPA reform will reduce settlement service costs and result in transfers to consumers from service providers. Entities that will suffer revenue losses under the proposed rule are usually those who are charging prices higher than necessary or are benefiting from the current system's market failure.

Note to Reader: A more comprehensive summary of the problems with the current mortgage shopping system and the benefits and market impacts of the proposed rule is provided in Section I of Chapter 3 of the RIA.

Appendix II.B. Problems With the Mortgage Shopping Process and the Current GFE

The current system for originating and closing mortgages is highly complex and suffers from several problems that have resulted in high prices for borrowers. Studies indicate that consumers are often charged high fees and can face wide variations in prices, both for origination and third-party settlement services. The main points are as follows:

- There are many barriers to effective shopping for mortgages in today's market. The process can be complex and can involve rather complicated financial trade-offs, which are often not fully and clearly explained to borrowers.
- Consumers often pay non-competitive fees for originating mortgages. Most observers believe that the market breakdown occurs in the relationship between the consumer and the loan originator—the ability of the loan originator to price discriminate among different types of consumers leads to some consumers paying more than other consumers.[36]
- There is convincing statistical evidence that yield spread premiums are not always used to offset the origination and settlement costs of the consumer. Studies, including a recent HUD-sponsored study of FHA closing costs by the Urban Institute, find that yield spread premiums are often used for the originator's benefit, rather than for the consumer's benefit.[37]
- Borrowers can be confused about the trade-off between interest rates and closing costs. It may be difficult for borrowers (even sophisticated ones but surely unsophisticated ones) to understand the financial trade-offs associated with discount points, yield spread premiums, and upfront settlement costs. While many originators explain this to their borrowers, giving them an array of choices to meet their needs, some originators may only show borrowers a limited number of options.
- There is also evidence that third-party costs are highly variable, indicating that there is much potential to reduce title, closing, and other settlement costs. For example, a recent analysis of FHA closing costs by the Urban Institute shows wide variation in title and settlement costs. There is not always an incentive in today's market for originators to control these costs. Too often, high third-party costs are simply passed through to the consumer. And consumers may not be the best shoppers for third-party service providers due to their lack of expertise and to the infrequency with which they shop for these services. Consumers often rely on recommendations from the real estate agent (in the case of a home purchase) or from the loan originator (in the case of a refinance as well as a home purchase).

Today's GFE. Today's GFE does not help the above situations, as it is not an effective tool for facilitating borrower shopping nor for controlling third-party settlement costs. The current GFE is typically comprised of a long list of charges, as today's rules do not prescribe a standard form and consolidated categories. Such a long list of individual charges can be overwhelming, often confuses consumers, and seems to provide little useful information for consumer shopping. The current GFE certainly does not inform consumers what the major costs are so that they can effectively shop and compare mortgage offers among different loan originators. The current GFE does not explain how the borrower can use the document to shop and compare loans. Also, the GFE fails to make clear the relationship between the closing costs and the interest rate on a loan, notwithstanding that many mortgage loans originated today adjust up-front closing costs due at settlement, either up or down, depending on whether the interest rate on the loan is below or above ''par.'' Finally, current rules do not assure that the ''good faith estimate'' is a reliable estimate of final settlement costs. As a result, under today's rules, the estimated costs on GFEs may be unreliable or incomplete, and final charges at settlement may include significant increases in items that were estimated on the GFE, as well as additional fees, which can add to the consumer's ultimate closing costs.

Thus, today's GFE is not an effective tool for facilitating borrower shopping or for controlling origination and third-party settlement costs. There is enormous potential for cost reductions in today's market, which is too often characterized by relatively high and highly variable charges for both origination and third-party services.

In addition, today's RESPA rules hold back efficiency and competition by acting as a barrier to innovative cost-reduction arrangements. While today's mortgage market is characterized by increased efficiencies and lower prices due to technological advances and other innovations, that is not the case in the settlement area where aggressive competition among settlement service providers simply does not always take place. Under current law, a provider's efforts to enter into volume arrangements with settlement service firms may be regarded as illegal, which likely impedes efforts to reduce the costs of third-party services. Similarly, existing RESPA regulations inhibit average cost pricing[38] (another example of a

[36] One could see price discrimination in a competitive market that was the result of different costs associated with originating loans for different applicants. For example, those who required more work by the originator to obtain loan approval might be charged more than those whose applications required little work in order to obtain an approval. The price discrimination we refer to in this paragraph and elsewhere in this analysis is not cost-based. It is the result of market imperfections, such as poor borrower information on alternatives that leads borrowers to accept loans at higher cost than the competitive level.

[37] See Section IV.D of Chapter 2 for a discussion of these studies.

[38] The charges reported on the HUD–1 are required to be the specific charge paid in connection with the specific loan for which the HUD–1 is filled out. Average cost pricing is the practice of charging all borrowers the same expected average charge for all the loans they work on. Average cost pricing requires less record

cost reduction technique). Thus, a framework is needed that would encourage competitive negotiations and other arrangements that would lead to lower settlement prices. The proposed GFE will provide such a framework.

Appendix II.C. Proposed Approach

Appendix II.C.1. Main Components of the Proposed GFE and HUD–1

The proposed GFE format simplifies the process of originating mortgages by consolidating costs into a few major cost categories.[39] The proposed GFE ensures that in brokered transactions, borrowers receive the full benefit of the higher price paid by wholesale lenders for a loan with a high interest rate; that is, so-called yield spread premiums. On both the GFE and HUD–1, the portion of any wholesale lender payments that arise because a loan has an above-par interest rate is passed through to borrowers as a credit against other costs. Thus, there is assurance that borrowers who take on an above-par loan receive funds to offset their settlement costs. The proposed GFE also includes a trade-off table that will assist consumers in understanding the relationship between higher interest rates and lower settlement costs.

HUD conducted consumer tests to further improve the GFE form in the 2002 proposed rule. Numerous changes were made to make the GFE more user-friendly. A summary page containing the key information for shopping was added; during the tests, consumers reported that the summary page was a useful addition to the GFE. The trade-off table, another component of the proposed GFE that consumers found useful, has also been improved. The end result is a form that consumers find to be clear and well written and, according the tests conducted, one that they can use to determine the least expensive loan. In other words, it is a shopping tool that is a vast improvement over today's GFE with its long list of fees that can change (i.e., increase) at settlement.

The proposed GFE includes a set of tolerances on originator and third-party costs: Originators must adhere to their own origination fees, and give estimates subject to a 10 percent upper limit on the sum of certain third-party fees. The tolerances on originator and third-party costs will encourage originators not only to lower their own costs but also to seek lower costs for third-party services.

The proposed rule would allow settlement service providers to seek discounts, including volume based discounts, for settlement services, providing the price charged on the HUD–1 is no more than the price paid to the third-party settlement service provider for the discounted service. This should lead to lower third-party settlement service prices. The proposed rule would allow service providers to use average cost pricing for third-party services they purchase so long as the average is calculated using an acceptable method and the charge on the HUD–1 is no greater than the average paid for that service. This will make internal operations for the loan originator simpler and less costly and competition among lenders will put pressure for these cost savings to be passed on to borrowers as well. The end result of all these changes should be lower third-party fees for consumers.

The HUD–1 has also been adjusted to ensure that the proposed GFE (a shopping document issued early in the process) and the HUD–1 (a final settlement document issued at closing) work well together. The layout of the proposed HUD–1 has new labeling of some lines so that each entry from the proposed GFE can be found on the proposed HUD–1 with the exact wording as on the GFE. This will make it much easier to determine if the fees actually paid at settlement are consistent with the GFE, whether the borrower does it alone or with the assistance of the settlement agent. The reduced number of HUD–1 entries that should result, as well as use of the same terminology on both forms should reduce the time spent by the borrower and settlement comparing and checking the numbers.

No sections of the current HUD–1 have been eliminated so the proposed HUD–1 should work for any settlement using the existing HUD–1. Given that there has been no significant change in the basic HUD–1 structure and layout, generating this new HUD–1 should not pose any problem for firms closing loans—in fact, the closing process will be much simpler given borrowers and closing agents can precisely link the information on the initial GFE to the information on the final HUD–1.

Appendix II.C.2. Estimates and Sources of Consumer Savings From the Proposed Rule

Overall Savings. Chapter 3 discusses the consumer benefits associated with the proposed GFE form and provides dollar estimates of consumer savings due to improved shopping for both originator and third-party services. Consumer savings were estimated under a variety of scenarios about originator and settlement costs.[40] In the base case, the estimated price reduction to borrowers comes to $8.35 billion, or 12.5 percent of the $66.7 billion in total charges (i.e., origination fees, appraisal, credit report, tax service and flood certificate and title insurance and settlement agent charges).[41] Thus, there is an estimated $8.35 billion in transfers from firms to borrowers from the improved disclosures and tolerances of the proposed GFE. This would represent savings of $668 per loan. Sensitivity analysis was conducted with respect to the savings projection in order to provide a range of estimates. Because title fees account for over 70 percent of third-party fees and because there is widespread evidence of lack of competition and overcharging in the title and settlement closing industry, one approach projected third-party savings only in that industry. This approach (called the ''title approach'') projected savings of $200 per loan in title and settlement fees. In this case, the estimated price reduction to borrowers comes to $8.38 billion ($670 per loan), or 12.6 percent of the $66.7 billion in total charges—savings figures that are practically identical to the base case mentioned above.[42] Other projections also showed substantial savings for consumers. As explained in Chapter 3, estimated consumer savings under a more conservative projection totaled $6.48 billion ($518 per loan), or 9.7 percent of total settlement charges. Thus, while consumer savings are expected to be $8.35 billion (or 12.5 percent of total charges) in the base case or $8.38 billion (12.7 percent of total charges) in the title approach, they were $6.48 billion (or 9.7 percent of total charges) in a more conservative sensitivity analysis. This $6.48–$8.38 billion ($518–$670 per loan) represents the substantial savings that can be achieved with the proposed GFE.

Industry Breakdown of Savings. Chapter 3 also disaggregates the sources of consumer savings into the following major categories: Originators with a breakdown for brokers and lenders, and third-party providers with a breakdown for the title and settlement industry and other third-party providers.[43] In the base case, originators (brokers and lenders) contribute $5.88 billion, or 70 percent of the $8.35 billion in consumer savings. This $5.88 billion in savings represents 14.0 percent of the total revenue of originators, which is projected to be $42.0 billion.[44] The $5.88 billion is divided between brokers, which contribute $3.53 billion, and lenders (banks, thrifts, and mortgage banks), which contribute the remaining $2.35 billion. The shares for brokers (60 percent) and lenders (40 percent) represent their respective shares of mortgage originations.

In the base case, third-party settlement service providers contribute $2.47 billion, or 30 percent of the $8.35 billion in consumer savings. This $2.47 billion in savings represents 10.0 percent of the total revenue of third-party providers, which is projected to be $24.738 billion.[45] The $2.47 billion is divided between title and settlement agents, which contribute $1.79 billion, and other

---

keeping and tracking for any individual loan since the numbers reported to the settlement agent need not be transaction specific. Average cost pricing is not permissible under RESPA because loan-specific prices are required.

[39] See the proposed GFE in Exhibit 3–B of Chapter 3.

[40] Throughout this Economic Analysis, the terms ''borrowers'' and ''consumers'' are often used interchangeably.

[41] Government fees and taxes and escrow items are not included in this analysis, as they are not subject to competitive market pressures.

[42] If the savings in title and settlement closing fees due to RESPA reform were only $150, then the estimated price reduction to borrowers comes to $7.76 billion, or 11.6 percent of the $66.7 billion in total charges.

[43] Readers are referred to Chapter 5 for a more detailed examination of the various component industries (e.g., title services, appraisal, etc.) as well as for the derivations of many of the estimates presented in this chapter.

[44] This assumes a 1.75 percent origination fee for brokers and lenders, which, when applied to projected originations of $2.4 trillion, yields $42.0 billion in total revenues from origination fees (both direct and indirect). See Steps (3)–(5) of Section VII.E.1 of Chapter 3 of the RIA for the explanation of origination costs. Sensitivity analyses are conducted for smaller origination fees of 1.5 percent and larger fees of 2.0 percent; see Step (21) in Section VII.E.4 of Chapter 3.

[45] See Step (7) of Section VII.E.1 of Chapter 3 of the RIA for the derivation of the $24.738 billion.

third-party providers (appraisers, surveyors, pest inspectors, etc.), which contribute $0.68 billion. Title and settlement agents contribute a large share because they account for 72.5 percent of the third-party services included in this analysis. In the title approach, title and settlement agents account for all third-party savings, which total $2.5 billion if per loan savings are $200 and $1.88 billion if per loan savings are $150.

Section II.C.4 of this appendix presents the revenue impacts on small originators and small third-party providers.

Sources of Savings: Lower Origination and Third-Party Fees. The Regulatory Impact Analysis presents evidence that some consumers are paying higher prices for origination and third-party services. The proposed GFE format in the proposed rule will improve consumer shopping for mortgages, which will result in better mortgage products, lower interest rates, and lower origination and third-party costs for borrowers.

- The proposed rule simplifies the process of originating mortgages by consolidating costs into a few major cost categories. This is a substantial improvement over today's GFE that is not standardized and can contain a long list of individual charges that encourages fee proliferation. This makes it easier for the consumer to become overwhelmed and confused. The consistent and simpler presentation of the proposed GFE will improve the ability of the consumer to shop.
- A GFE with a summary page, which includes the terms of the loan, will make it to clear to the consumer whether they are comparing similar loans.
- A GFE with a summary page will make it simpler for borrowers to shop. The higher reward for shopping, along with the increased ease with which borrowers can compare loans, should lead to more effective shopping, more competition, and lower prices for borrowers.
- The proposed GFE makes cost estimates more reliable by applying tolerances to the figures reported. This will reduce the all too frequent problem of borrowers being surprised by additional costs at settlement. With fees firmer under the proposed GFE, shopping is more likely to result in borrowers saving money when they shop.
- The proposed GFE will disclose yield spread premiums and discount points in brokered loans prominently, accurately, and in a way that should inform borrowers how they may be used to their advantage. Both values will have to be calculated as the difference between the price of the loan and its par value. Their placement in the calculations that lead to net settlement costs will make them very difficult to miss. That placement should also enhance borrower comprehension of how yield spread premiums can be used to reduce up-front settlement costs. Tests of the form indicate that consumers can determine the cheaper loan when comparing a broker loan with a lender loan.
- The proposed GFE will better inform consumers about their financing choices by requiring that lenders present the different interest rate and closing cost options available to them. For example, consumers will better understand the trade-offs between reducing their closing costs and increasing the interest rate on the mortgage.
- The proposed rule allows settlement service providers to seek discounts, including volume based discounts, for settlement services. In addition, the rule allows service providers to use average cost pricing for third-party services they purchase.
- The above changes and the imposition of tolerances on fees will encourage originators to seek discounts, which should lower settlement service prices. The tolerances will lead to well-informed market professionals either arranging for the purchase of the settlement services or at least establishing a benchmark that borrowers can use to start their own search. Under either set of circumstances, this should lead to lower prices for borrowers than if the borrowers shopped on their own, since the typical borrower's knowledge of the settlement service market is limited, at best.

Appendix II.C.3. Savings and Transfers, Efficiencies, and Costs

As explained above, it is estimated that borrowers would save $8.35 billion in origination and settlement charges. This $8.35 billion represents transfers to borrowers from high priced producers, with $5.88 billion coming from originators and $2.47 billion from third-party settlement service providers. In addition to the transfers, there are efficiencies associated with the rule as well as costs.

Mortgage applicants and borrowers realize $1,073 million savings in time spent shopping for loans and third-party services. Loan originators save $1,404 million in time spent with shoppers, in efforts spent seeking out vulnerable borrowers, and from average cost pricing. Third-party settlement service providers save $113 million in time spent with shoppers. Some or all of the $1,404 million and $113 million in efficiency gains have the potential to be passed through to borrowers through competition.

The total one-time compliance costs to the lending and settlement industry of the proposed GFE and HUD–1 are estimated to be $570 million, $390 million of which is borne by small business. These costs are summarized below. Total recurring costs are estimated to be $1.231 billion annually or $98.48 per loan. The share of the recurring costs on small business is $548 million. This chapter examines in greater detail the compliance and other costs associated with the proposed GFE and HUD–1 forms and its tolerances.

The proposed GFE has some features that would increase the cost of providing it and some that would decrease the cost. Practically all of the information required on the GFE is readily available to originators, suggesting no additional costs. The fact that there are fewer numbers and less itemization of individual fees suggests reduced costs. On the other hand, there could be a small amount of additional costs associated with the trade-off table but that is not clear. Thus, while it is difficult to estimate, it appears that there could be a net of zero additional costs. However, if the proposed GFE added 10 minutes to the time it takes to handle the forms today, annual costs would rise by $255 million ($12 per application or $20 per loan). (See Section VII.C.1 of this appendix.)

The presence of tolerances will lead to some additional costs to originators of making additional arrangements for third parties to provide settlement services. If the average loan originator incurs an average of 10 minutes per loan of effort making third-party arrangements to meet the tolerances, then the total cost to originators of making third-party arrangements to meet the tolerance requirements comes to $300 million ($24 per loan). (See Section Appendix VII.E.2.)

In addition to the recurring costs of the proposed GFE, there will be one-time adjustment costs of $401 million in switching to the new form. Loan originators will have to upgrade their software and train staff in its use in order to accommodate the requirements of the new rule. It is estimated that the software cost will be $33 million and the training cost will be $58 million, for a total of $91 million (see Section Appendix III.B.1). Once the new software is functioning, the recurring costs of training new employees in its use and the costs associated with periodic upgrades simply replace those costs that would have been incurred doing the same thing with software for the old rule. They represent no additional costs of the new rule. Similarly, there will be a one-time adjustment cost for legal advice on how to deal with the changes related to the new GFE. The one-time adjustment cost for legal fees is estimated to be $116 million (see Appendix III.B.2). Once the adjustment has been made, the ongoing legal costs are a substitute for the ongoing legal costs that would have been incurred under the old rule and do not represent any additional burden.

Finally with respect to the GFE, employees will have to be trained in the new GFE beyond the software and legal training already mentioned. This one time adjustment cost is estimated to be $193 million (see Section Appendix III.B.3). Again, once the transition expenses have been incurred, any ongoing training costs are a substitute for the training costs that would have been incurred anyway and do not represent an additional burden.

There will be recurring costs of the new HUD–1 on the settlement industry arising from the addition of the closing script. Requiring the script would impose a cost on the settlement industry only when it increases the average time spent to complete a settlement. Settlement agents would be obliged to collect data from the GFE, fill out the script, read it to the borrower, and answer any questions engendered by the script. The typical agent will perform this kind of work regardless of whether they are required to do so. A script only standardizes the explanation of the correspondence between the GFE and the HUD–1 forms. It is conceivable that the burden imposed on the average conscientious agent is very modest. However, to be cautious, we assume that the script would lead to an additional forty-five minutes spent on the average settlement. The opportunity cost of that time to the settlement firm would be $54 (derived from a $150,000 fully loaded salary). The total cost of the script in a normal year (12.5 million originations) would be $676 million and $838 million in a high volume year (15.5 million originations). (See Section VII.C.2 of this appendix for a lengthier discussion.)

There will be one-time adjustment costs of $169 million in switching to the new HUD–1 form and its new addendum, the standardized closing script. Settlement firms will have to upgrade their software and train staff in its use in order to accommodate the requirements of the new rule. It is estimated that the software cost will be $14 million and the training cost will be $48 million, for a total of $62 million (see Section Appendix VII.B.). Once the new software is functioning, the recurring costs of training new employees in its use and the costs associated with periodic upgrades simply replace those costs that would have been incurred doing the same thing with software for the old rule. They represent no additional costs of the new rule.

Similarly, there will be a one-time adjustment cost for legal advice on how to deal with the changes related to the new HUD–1. The one-time adjustment cost for legal fees is estimated to be $37 million (see Section Appendix VII.B.). Once the adjustment has been made, the ongoing legal costs are a substitute for the ongoing legal costs that would have been incurred under the old rule and do not represent any additional burden.

Finally, employees will have to be trained in the new HUD–1 beyond the software and legal training already mentioned. This one time adjustment cost is estimated to be $71 million (see Section Appendix VII.B.). Again, once the transition expenses have been incurred, any ongoing training costs are a substitute for the training costs that would have been incurred anyway and do not represent an additional burden.

The consumer savings, efficiencies and costs associated with the proposed GFE are discussed further in the Appendix and in Chapter 3 of the RIA. A summary of the compliance costs for the base case of 12.5 million loans annually is presented below in Table A–1.

TABLE A–1.—COMPLIANCE COSTS OF THE PROPOSED RULE (IF 12.5 MILLION LOANS ANNUALLY)

	One-time compliance costs incurred during the first year (in millions)		Recurring compliance costs (in millions annually)		$ cost per loan
	All firms	Small firms	All firms	Small firms	
GFE	$401	$280	$555	$290	$44.40
HUD–1	169	110	676	258	54.08
Total	570	390	1,231	548	98.48

The costs of the closing script are included in the HUD–1 costs. Note that all of the recurring costs from the HUD–1 stem entirely from the required closing script.

Appendix II.C.4. Alternatives Considered To Make the GFE More Workable for Small and Other Businesses

Chapter 3 discusses the many comments that HUD received on the GFE in the 2002 proposed rule and in the 2005 RESPA Reform Roundtables. Chapter 4 discusses alternatives. The most basic alternative was to make no change in the current GFE. Some commenters, particularly those who favored packaging, argued that the current GFE should be left in place while packaging was given a chance to work. The proposed rule does allow the current GFE to be used for one year after the proposed GFE is introduced. This one-year adjustment period responds to lenders' comments that there would be significant implementation issues with switching to a proposed GFE.

The main alternative concerning small businesses considered the brokers' argument that they were disadvantaged by the reporting of yield spread premiums. HUD improved the proposed GFE to ensure that there will not be any anti-competitive impacts on the broker industry. A summary page was added that presents the key cost figures for borrower shopping, that does not report yield spread premiums, and that provides identical treatment for brokers and lenders. The proposed GFE adds language that clarifies how yield spread premiums reduce the upfront charge that borrowers pay.

HUD changed the GFE to make it more workable for small lenders and brokers. Some examples of the changes are the following:

• In response to concerns expressed by lenders and brokers about their ability to control third-party costs and meet the specified tolerances in the 2002 proposed rule, the proposed rule clarifies that ''zero tolerance'' does not pertain in ''unforeseeable circumstances'' beyond the originator's control. The tolerance for fees for lender-required, lender-selected third-party services was also increased from zero percent to 10 percent. The sum of the fees to which the ten percent tolerance applies may not exceed the initial sum by more than ten percent. However, individual fees in this category may increase by more than ten percent.

• Consistent with the above, the rule clarifies the definition of ''unforeseeable circumstances'' to include circumstances that could not be reasonably foreseen at the time of GFE application—examples include the need for a second appraisal or flood insurance.

• The definition of an application was changed to be consistent with the way consumers and lenders operate today—a ''GFE application'' would serve as a shopping application and a ''mortgage application'' would be submitted once a shopper chooses a particular loan originator, and would resemble the standard application in today's market and be the basis for full underwriting.

• The proposed rule clarifies that only the ''mortgage application'' would be subject to Regulations B (ECOA) and C (HMDA), which is the current situation today.

• HUD reduced the guarantee period for tolerances to 10 business days, which gives borrowers ample time to shop and does not impose large operational and hedging costs on lenders and brokers (as 30 days might have).

• Lenders and brokers objected to the requirement that they calculate the Annual Percentage Rate (APR) on the GFE; for a variety of reasons, HUD dropped the APR from the proposed GFE. They also disagreed with splitting out the broker and lender portions of the origination fee on the back page of the GFE; HUD dropped that from the proposed GFE.

The above changes address a number of practical and implementation problems raised by lenders and brokers about the proposed GFE. The changes make the proposed GFE easier to use for small lenders and brokers.

Alternatives. This chapter and Chapter 4 discuss other major alternatives that HUD considered, including single packaging, dual packaging, and a Settlement Service Package. These chapters discuss the pros and cons of these alternatives and why HUD decided not to include them in this proposed rule. For example, HUD did consider the option of offering a Mortgage Package Offer (MPO, or single packaging) with a Section 8 safe harbor in combination with the proposed GFE. HUD rejected this alternative for several reasons. First, HUD included tolerances in the proposed GFE, which will encourage lenders to negotiate with third-party providers in order to reduce their costs. Second, this proposed rule encourages volume discount arrangements (one of the cost-reduction features of single packaging), which will also lead to more competitive third-party prices. Third, the proposed rule allows lenders and other service providers to average cost price (another cost-reduction feature of single packaging). Fourth, the proposed GFE itself is a much improved shopping document over the existing GFE; for example, individual fees are consolidated into broad categories and a summary, first page provides the shopper with key information to select the least expensive loan package. Thus, the proposed GFE already includes many of the cost-reducing features that would supposedly be offered by packing. Finally, this is all accomplished without having to offer a Section 8 exemption to the industry.

Appendix II.C.5 Market and Competitive Impacts on Small Businesses From the Proposed Rule

Transfers from Small Businesses. It is estimated that $4.13 billion, or 49.5 percent of the $8.35 billion in consumer savings comes from small businesses, with small originators contributing $3.01 billion and small third-party firms, $1.13 billion.[46] Within the small originator group, most of the transfers to consumers come from small brokers ($2.47 billion, or 82 percent of the $3.01 billion); this is because small firms account for most of broker revenues but a small percentage of lender revenues. Within the small third-party group, most of the transfers come from the title and closing industry ($0.68 billion, or 60 percent of the $1.13 billion), mainly because this industry accounts for most third-party fees. In the title approach, small title and settlement closing companies account for $0.95 billion of the $2.5 billion in savings. Section VII.E.2 of Chapter 3 of the Regulatory Impact Analysis IA explains the steps in deriving these revenue impacts on small businesses, and Section VII.E.4 of Chapter 3 reports several sensitivity analyses around the estimates. In addition, Chapter 5 of the RIA provides more detailed revenue impacts for the various component industries.[47]

The summary bullets in Section Appendix II.C.2 highlight the mechanisms through which these transfers are expected to happen. Improved understanding of yield spread premiums, discount points, and the trade-off between interest rates and upfront costs; improved consumer shopping among originators; more aggressive competition by originators for settlement services; and increased competition associated discounting—all will lead to reductions in both originator and third-party fees. As noted earlier, there is substantial evidence of non-competitive prices charged to some in the origination and settlement of mortgages. Originators (both small and large) and settlement service providers (both small and large) that have been charging high prices will experience reductions in their revenues as a result of the proposed GFE. There is no evidence that small businesses have been disproportionately charging high prices; for this reason, there is no expectation of any disproportionate impact on small businesses from the proposed GFE. The revenue reductions will be distributed across firms based on their non-competitive price behavior.

Small Brokers.[48] The main issue raised by the brokers concerned the treatment in the 2002 proposed rule of yield spread premiums on the proposed Good Faith Estimate. This was also the main small business issue with the 2002 proposed GFE since practically all brokers qualify as small businesses. As explained above, the current proposed rule addresses the concern expressed by brokers that the reporting of yield spread premiums in the 2002 proposed rule would disadvantage them relative to lenders. The Department hired forms development specialists, the Kleimann Communication Group, to analyze, test, and improve the forms. They reworked the language and presentation of the yield spread premium to emphasize that it offsets other charges to reduce up-front charges, the cash needed to close the loan. The subjects tested seemed to like the table on page 3 of the form that shows the trade-off between the interest rate and up-front charges. It illustrates how yield spread premiums can reduce upfront charges. There is the new summary page designed to simplify the digestion of the information on the form by including only summary information from page two: The adjusted origination charge, the sum of all other charges, and the total. This is the first page any potential borrower would see. It contains only the essentials for comparison-shopping and is simple: A standard set of yes–no questions describing the loan and a very simple summary of costs and the bottom line. Yield spread premiums are never mentioned here. Lender and broker loans get identical treatment on page 1. A mortgage shopping chart has been added as a last page of the GFE, to help borrowers comparison shop. Arrows were added to focus the borrower on overall charges, rather than one component. All of these features work against the borrower misinterpreting the different required presentation of loan fees required of brokers vis-à-vis lenders.

HUD has redesigned the proposed GFE form to focus borrowers on the right numbers so that competition is maintained between brokers and lenders. The forms adopted in the proposed rule were tested on hundreds of subjects. The tests indicate that borrowers who comparison shop will have little difficulty identifying the cheapest loan offered in the market whether from a broker or a lender.

The customer outreach function that brokers perform for wholesale lenders is not going to change with RESPA reform. Wholesale lending, which has fueled the rise in mortgage originations over the past ten years, will continue to depend on brokers reaching out to consumer customers and supplying them with loans. Brokers play the key role in the upfront part of the mortgage process and this will continue with the proposed GFE.

RESPA reform is also not going to change the basic cost and efficiency advantages of brokers. Brokers have grown in market share and numbers because they can originate mortgages at lower costs than others. There is no indication that their cost competitiveness is going to change in the near future. Thus, brokers, as a group, will remain highly competitive actors in the mortgage market, as they have been in the past.

While there is no evidence to suggest any anti-competitive impact, there will be an impact on those brokers who are charging non-competitive prices. And there is convincing evidence that some brokers (as well as some lenders) overcharge consumers (see studies reviewed in Chapter 2). As emphasized throughout the Regulatory Impact Analysis, the proposed GFE will lead to improved and more effective consumer shopping, for many reasons—the proposed GFE is simple and easy to understand, it includes reliable cost estimates, it effectively discloses yield spread premiums and discounts in brokered loans without disadvantaging brokers, it ensures that consumers are shown options, and it explains the trade-off between closing costs and yield spread premiums. This increased shopping by consumers will reduce the revenues of those brokers who are charging non-competitive prices. Thus, the main impact on brokers (both small and large) of the proposed rule will be on those brokers (as well as other originators) who have been overcharging uninformed consumers, through the combination of high origination fees and yield spread premiums.[49] As noted above, small brokers are expected to experience $2.47 billion in reduced fees.

Section VIII.A of Chapter 3 of the RIA discusses other concerns raised by brokers about the 2002 proposed GFE, such as the following:

1. Brokers were concerned about their ability to control costs and meet the specified tolerances in the 2002 proposed rule. As explained above, the proposed rule made several adjustments to the tolerance rules and clarified when tolerances would or would not be in effect.

2. Brokers supported a generic trade-off table but the Department concluded, based on consumer testing, that a customized trade-off chart was essential for increasing consumer understanding of the complex yield spread premium issue.

3. Brokers disagreed with splitting out the broker and lender portions of the origination fee on the back page of the GFE; HUD has dropped that on the 2007 proposed GFE.

4. Brokers did not agree with the 30-day shopping period for the GFE; HUD reduced that to 10 days, which should provide adequate time for consumers to shop.

5. Brokers raised objections to having brokers calculate the Annual Percentage Rate (APR) on the GFE; for a variety of reasons, HUD has dropped the APR from the GFE.

To a large extent, brokers raised many of the same implementation issues voiced by lenders in their comments. The changes that HUD made in the 2007 proposed rule will

---

[46] In the more conservative scenario of $6.48 billion in consumer savings, small businesses would account for $3.21 billion of the transfers to consumers, with small originators accounting for $2.36 billion, and small third-party providers, $0.84 billion.

[47] In Chapter 5 of the RIA, see Section II for brokers, Section III for the four lender groups (commercial banks, thrifts, mortgage banks, and credit unions), Section IV for the various title and settlement groups (large insurers, title and settlement agents, lawyers, and escrow firms), Section V.A for appraisers, Section V.B for surveyors, Section V.C for pest inspectors, and Section V.D for credit bureaus.

[48] Practically all (98.9%) of the 30,000–44,000 brokers qualify as a small business. The Bureau of Census reports that small brokers account for 70% of industry revenue.

[49] As explained throughout this chapter, it is anticipated that market competition, under this proposed GFE approach, will have a similar impact on those lenders (non-brokers) who have been overcharging consumers through a combination of high origination costs and yield spread premiums.

make the GFE more workable for small brokers and small lenders.

Small Lenders. Lenders include mortgage banks, commercial banks, credit unions, and thrift institutions.[50] There are over 10,000 lenders that would be affected by the RESPA rule, as well as almost 4,000 credit unions that originate mortgages. While two-thirds of the lenders qualify as a small business (as do four-fifths of the credit unions), these small originators account for only 23 percent of industry revenues. Thus, small lenders (including credit unions) account for only $540 million of the projected $2.35 billion in transfers from lenders.[51] Section VIII.B of Chapter 3 of the RIA provides a detailed discussion of the anticipated impacts of the rule on lenders, and the pros and cons of the various policy alternatives that the Department considered.

In general, there was less concern expressed by lenders (as compared with brokers) about potential anti-competitive impacts of the GFE on small businesses. Small lenders—relative to both brokers and large lenders—will remain highly competitive actors in the mortgage market, as they are today. Small mortgage banks, community banks and local savings institutions benefit from their knowledge of local settlement service providers and of the local mortgage market. Nothing in the 2007 proposed GFE rule changes that.

For the most part, lenders supported the packaging concept but wanted to delay the enhanced GFE while packaging was given a chance to work. As explained above, HUD allows a 12-month implementation period during which the current GFE could be used, which should give lenders time to adjust their computer systems and train employees to use the proposed GFE.

Lenders had numerous comments on most aspects of the 2002 proposed GFE form—some of them dealing with major issues such as the difficulty in predicting costs within a three day period and many dealing with practical and more technical issues. HUD responded to many of the issues and concerns raised by lenders; Sections V, VI, and VIII of Chapter 3 discuss lenders' comments and HUD's response.

Some lenders were concerned about their ability to produce firm cost estimates (even of their own fees) within a three-day period, given the complexity of the mortgage process. Lenders wanted clarification on their ability to make cost adjustments as a result of information they gain during the full underwriting process. The tolerances in the proposed rule require that lenders play a more active role in controlling third-party costs than they have in the past. However, some lenders emphasized that they have little control over fees of third-party settlement providers, while others seem to not anticipate problems in this regard. As explained in I.B above, the proposed rule made several adjustments to the tolerance rules, which should make them workable for lenders. In addition, the proposed rule allows volume discounting and average cost pricing, which should help lenders reduce their costs. Practically all lenders wanted clarification on the definition of application, and HUD did that, along the same lines that lenders suggested in their comments.

There will be an impact on those lenders (both large and small) who are charging non-competitive prices. Improved consumer shopping with the proposed GFE will reduce the revenues of those lenders who are charging non-competitive prices. Thus, as with brokers, the main negative impact on lenders (both small and large) of the proposed GFE will be on those lenders who have been overcharging uninformed consumers.

Small Title and Settlement Firms. The title and settlement industry—which consists of large title insurers, title agents, escrow firms, lawyers, and others involved in the settlement process—is expected to account for $1.79 billion of the $2.47 billion in third-party transfers under the proposed GFE. Within the title and settlement group, small firms are expected to account for 38.1 percent ($0.68 billion) of the transfers, although there is some uncertainty with this estimate.[52] Step (8) of Section VII.E of Chapter 3 conducts an analysis that projects all of the consumer savings in third-party costs coming from the title industry; evidence suggests there are more opportunities for price reductions in the title industry, as compared with other third-party industries. In this case, consumer savings in title costs ($150–$200 per loan) ranged from $1.88 billion to $2.50 billion. To a large extent, the title and closing industry is characterized by local firms providing services at constant returns to scale. The demand for the services of these local firms will continue under the proposed GFE.

Section VIII.C of Chapter 3 summarizes the key competitive issues for this industry with respect to the proposed rule. As noted there, the overall competitiveness of the title and closing industry should be enhanced by the RESPA rule. Chapters 2 and 5 and Section III.E of Chapter 3 of the Regulatory Impact Analysis provide evidence that title and closing fees are too high and that there is much potential for price reductions in this industry. Increased shopping by consumers, as well as increased shopping by loan originators to stay within their tolerances, will reduce the revenues of those title and closing companies that have been charging non-competitive prices.[53] Excess charges will be reduced and competition will ensure that reduced costs are passed through to consumers.

The title industry argued that greater itemization was needed in order for consumers to be able to adequately comparison shop among estimates. HUD's view is that the consolidated categories on the proposed GFE form provide consumers with the essential information needed for comparison-shopping. Itemization encourages a long list of fees that confuse borrowers.

It is important to emphasize that the services of the title and closing industry, as well as other third-party industries (appraisers, surveyors, and pest inspectors), are local in nature and are performed near or at the site. Local firms have advantages of knowledge and networks of clients, as well as transportation cost advantages. As explained in Chapter 3, these advantages of small, locally based firms will not be negatively impacted by the new Good Faith Estimate. In fact, RESPA reform should open up opportunities for efficient third-party firms to expand their operations.

Appendix III. Statement of Need for and Objectives of the Rule[54]

Acquiring a mortgage is one of the most complex transactions a family will ever undertake. The consumer requires a level of financial sensibility to fully understand the product. For example, consider the trade-off between the yield spread premium and interest rate payments. Borrowers do not have access to the rate sheets that describe this trade-off. Indeed, many consumers may not even understand that there is a trade-off. To further complicate matters, the mortgage industry is continuously evolving: The range and complexity of products expands every year. Because consumers borrow fairly infrequently, the average borrower will be at an extreme informational disadvantage compared to the lender. To exacerbate this situation, the typical homebuyer may be rushed and easily steered into a bad loan because they are under pressure to make an offer on a home. This is especially the case for first-time homebuyers who will not be as likely to challenge lenders, whom they may view as unquestionable experts.

Closing costs (lender fees and title charges) add to the borrower's confusion. They are not as significant as the loan itself and total on average approximately four percent of the loan amount. However, the direct lender fees and the title charges are perhaps just as perplexing to the consumer. First, the multiplicity of fees is confusing (see Exhibits 1–3 of Chapter 3 for a list of the different names of upfront lender fees and settlement charges). The purpose of every fee and title charge is likely to be neither understood nor questioned by the average first-time homebuyer, who may be intimidated by the formality of the transaction. Second, to add to the confusion and uncertainty, even once the charges have been agreed upon, they are subject to change until the day of closing.

[50] While it is recognized that the business operations and objectives of these lender groups can differ—not only between the groups (a mortgage banker versus a portfolio lender) but even within a single group (a small community bank versus a large national bank)—they raised so many of the same issues that it is more useful to address them in one place.

[51] Section III of Chapter 5 describes the characteristics of these component industries (number of employees, size of firms, etc.), their mortgage origination activity, and the allocation of revenue impacts between large and small lenders. That section also explains that the small business share of revenue could vary from 20 percent to 26 percent.

[52] Section IV of Chapter 5 describes the component industries and estimates the share of overall industry revenue going to small businesses.

[53] The reasons why the proposed GFE and its tolerances will lead to improved and more effective shopping for third-party services by consumers and loan originators has already been discussed, and need not be repeated here.

[54] For a detailed discussion of problems with the current system, and thus the need for this proposed rule, see Sections IV and V of Chapter 2 and Sections I and VII of Chapter 3.

Such informational asymmetries between the buyer and seller impede the ability of the consumer to be an effective shopper and negotiator.

Consumers have strong incentives to ensure that they are getting the best deal possible on a mortgage loan and the associated third-party settlement costs, but poorly-informed decisions have drastic consequences. First, the household itself will lose by paying more for housing and possibly by ruining their credit history in the event of default. Second, market imperfections stemming from information asymmetries may stand in the way of achieving one of this administration's domestic priorities: Expansion of homeownership. There is a wide range of positive economic externalities from homeownership that have been investigated in the empirical housing economics literature. These include household saving, wealth accumulation, property improvements, a more pleasing urban environment, an increase in political activity, a reduction of crime, better child outcomes, and a positive impact on the labor supply of women. The average loan amount is 3.5 times a household's income: Even minor inefficiencies in this market will have sizeable impacts on the U.S. economy.

The current GFE format contains a long list of individual charges that can be overwhelming, often confuses consumers, and seems to provide little useful information for consumer shopping. Current RESPA regulations have led to a proliferation of charges that makes consumer shopping and the mortgage settlement process both difficult and confusing, even for the most informed shoppers. Long lists of charges certainly do not highlight the bottom-line costs so consumers can shop and compare mortgage offers among different originators. In addition, under today's rules, the estimated costs on GFEs may be unreliable or incomplete, or both, and final charges at settlement may include significant increases in items that were estimated on the GFE, as well as additional unexpected fees, which can add substantially to the consumer's ultimate closing costs. The process of shopping for a mortgage can also involve complicated financial trade-offs, which are not always clearly explained to borrowers. Today's GFE is not an effective tool for facilitating borrower shopping nor for controlling origination and third-party settlement costs.

The potential for cost reductions in today's market is also indicated by studies showing relatively high and highly variable charges for third-party services, particularly for title and closing services that account for the major portion of third-party fees. There is not enough incentive for loan originators to control settlement costs by negotiating lower costs from third-party providers; rather, they too often simply pass through increases in third-party costs to consumers. Because of their lack of expertise, consumers may not be the best shoppers for third-party services providers, leaving them to rely on recommendations from real estate agents and lenders. Thus, a framework is needed that would encourage competitive negotiations and other arrangements that would lead to lower third-party settlement prices.

Current RESPA regulations are acting as a major barrier to competition and lower settlement costs. Today's mortgage market is increasingly characterized by the introduction of efficiency enhancing improvements such as automated underwriting systems and, through competition, these improvements are leading to lower prices for consumers. But the one area where efficiencies and competition are being held back is the production and pricing of settlement services. Under current law, a provider's efforts to enter into volume arrangements with settlement service firms may be regarded as illegal, which may impede the cost-reducing arrangements to deliver third-party settlement services. Similarly, average cost pricing (another cost reduction technique) is inhibited by existing RESPA regulations.

The goal of HUD's proposed RESPA reform is to even the playing field. The rule will accomplish this by requiring lenders to provide consumers information that lenders already have in a format that is transparent. One of the major inefficiencies of imperfect information is the costs of acquiring information. The proposed RESPA reform will go a long way toward educating consumers. The first page of the new GFE presents a brief summary of the terms of the loan that would warn prospective borrowers of potentially expensive aspects of the loan including loan amount, maximum interest rate, prepayment penalties, and the total estimated settlement charges. The second page provides more detail on the charges for loan origination and other settlement services. The third page provides a trade-off table so that consumers will learn the relationship between the interest rate and the yield-spread premium. The fourth page includes a table so that the consumer can take notes on alternative loan offers and thus comparison shop. Tolerances will limit how much settlement charges can vary once the GFE has been made and the closing script will serve to double-check the GFE and provide a summary of the key terms of the borrower's loan. The proposed rule also allows settlement service providers to use average cost pricing and volume discounting, making their business operations simpler and less costly. It is expected that the proposed GFE will encourage shopping, increase efficiency, lower housing costs, and promote the purchase of loans that are more suited to a household's needs.

Empirical Evidence of Price Discrimination. Studies indicate that consumers are often charged relatively high fees and can face wide variations in settlement prices, both for origination and third-party settlement services. Chapter 2 offers convincing evidence that not only do borrowers find it difficult to comparison shop in today's mortgage market, but that they are all too often charged excessive prices. The enormous potential for cost reductions in today's market is indicated by studies showing that yield spread premiums do not always offset consumers' origination costs. Studies show that consumers are, in effect, charged relatively high prices in some transactions involving yield-spread premiums, and that the mortgage market is characterized by ''price dispersion.'' In other words, some borrowers get market price deals, but other borrowers do not. Studies show that less informed and unsuspecting borrowers are particularly vulnerable in this market. But given the fact that a borrower may be more interested in the main transaction (the home purchase), even more sophisticated borrowers may not shop aggressively for the mortgage or may not monitor the lending transaction very closely.

The (2007a) conducts an analysis of 5,926 non-subsidized FHA loans. The median total loan closing cost is $5,334. Total charges are composed of loan charges ($3,392), title charges ($1,267), and other third party charges ($574). It is apparent from the distribution presented below that there is significant variation in closing costs. The ratio of what the 75th percentile pays to what the 25th percentile pays is 1.7 for total closing costs, 2.0 for total loan charges, 2.4 for the yield-spread premium (indirect loan fee), 2.9 for direct loan fees, 1.7 for title charges, and 1.6 for other third-party charges. These results are shown below in Table A–2.

TABLE A–2.—DISTRIBUTION OF CATEGORIES OF CLOSING COSTS

[Exhibit 11, Urban Institute 2007a]

Series	5th percentile	25th percentile	50th percentile (median)	75th percentile	95th percentile
.					
Total Closing Cost	$2,663	$4,045	$5,334	$6,889	$10,183
Total Loan Charges	1104	2,310	3,392	4,714	7,394
Yield-spread premium (indirect) loan fee	250	1,249	2,041	3,016	4,658
Direct loan fees	21	683	1,387	2,008	3,696
Total Title Charges	666	953	1,267	1,652	2,407
Total Other Third-Party Charges	293	469	574	744	1,097

The greatest degree of variation appears in the lender fees. Since total loan charges are correlated with loan amount, it would be useful to examine the distribution of closing costs as a percentage of loan amounts to ascertain whether the variation in fees is still present. There is slightly less variation when measured as a percentage but it is still substantial: The ratio of what the 75th percentile pays as a percentage of the loan to what the 25th percentile pays is 1.8 for total loan charges, 2.1 for the yield spread premium (indirect loan fee), and 2.4 for direct loan fees. (See Table A–3 below.)

TABLE A–3.—DISTRIBUTION OF CATEGORIES OF CLOSING COSTS AS A PERCENTAGE OF LOAN AMOUNT

[Calculated by HUD from the data used by Urban Institute 2007a]

Series	5th percentile	25th percentile	50th percentile (median)	75th percentile	95th percentile
Total Closing Cost	2.9	4.1	5.1	6.4	8.9
Total Loan Charges	1.3	2.4	3.2	4.2	6.2
Yield-spread premium (indirect) loan fee	0.3	1.3	2.0	2.7	3.8
Direct loan fees	0.0	0.8	1.3	1.8	3.3
Total Title Charges	0.6	0.9	1.2	1.6	2.3
Total Other Third-Party Charges	0.2	0.4	0.6	0.8	1.4

It is apparent that half of the borrowers pay loan charges equal or greater than 3.2% of their loan amount; one-quarter pay loan charges of at least 4.2% of their loan amount; and five percent pay loan charges of at least 6.2% of their loan amount. The variation is similar for title charges and other third-party charges. Half of the borrowers pay total closing costs equal or greater than 5.1% of their loan; one-quarter pay closing costs of at least 6.4% of their loan amount, and five percent pay closing costs of at least 8.9% of their loan amount.

HUD believes that these data provides strong indications of large price dispersion and thus price discrimination. Price discrimination will always lead to a loss in consumer surplus and unless price discrimination is perfect, it will also lead to a loss in social welfare. It should also be noted that if the variation of fees and charges paid is greater than the actual costs of providing the services, then that constitutes evidence of a violation of RESPA, which explicitly prohibits mark-ups.

First, in a competitive market the price of the good should depend on its quality and not to whom and how it is sold. If there is dispersion because the negotiations are face-to-face, this would suggest that the nature of the market exacerbates the consumer's informational disadvantage. Indeed, there is strong evidence that individuals pay different prices for reasons other than how costly service provisions will be. An Urban Institute report (2007b) finds that African Americans pay an additional $415 for their loans and that Latinos pay an additional $365 (after taking into account borrower differences such as credit score and loan amount). These loans are not subprime loans but standard FHA loans. Other researchers have found similar results: Jackson and Berry (2002, see the Regulatory Impact Analysis for reference) find that mortgage brokers charge African-Americans (by $474) and Hispanics (by $580) substantially more for settlement services than other borrowers. Discrimination by race or ethnicity is not economically efficient and would not survive in a perfectly competitive market.

Second, reconsider the yield-spread premium. We mentioned that this is one of the elements of a mortgage that a consumer is not likely to understand. The yield-spread premium is compensation to the broker for selling a loan with a higher interest rate. Thus, as the interest rate rises so should the yield-spread premium. This relationship appears to hold in the data analyzed. The broker earns income from two sources: A yield-spread premium that is paid by the lender and fees that are paid by the consumer. However, the burden of the yield-spread premium is on the consumer, who pays a higher interest rate for loans with a higher yield-spread premium. If consumers were perfectly informed, there would be a negative one-to-one relationship between up-front fees and the yield-spread premium. They simply represent two different ways of compensating the broker for the effort required to originate a loan.

The Urban Institute (2007b) finds no clear trade-off between the yield-spread premium and upfront cash payments. (This analysis is based on loans with interest rates of over 7 percent. In this sample, there are 4,603 loans; the average upfront cash is $1,179 with a standard deviation of $1,125; and the average YSP is $2,365 with a standard deviation of $1,044.) There is even a slight positive relationship between the upfront cash divided by the loan and the YSP divided by the loan amount. That is, upfront cash as a percentage of loan amount increases with the YSP as a percentage of loan amount. FHA borrowers appear to get no benefit from YSPs on brokered loans with coupon rates above 7 percent. Such a relationship is contrary to what one would expect in a market where there were only minor imperfections. Further evidence is from Jackson and Berry (2002) who studies only brokered transactions, a description of which can be found in Section IV.D.2 of Chapter 2 of the Regulatory Impact Analysis. They find that the problem of price dispersion occurs when yield spread premiums are present, because in these situations there is no single price for broker services: ''Most borrowers pay more than 1.5 percent of loan value; more than a third pay more than 2.0 percent of loan value; roughly ten percent pay more than 3.5 percent of loan value.'' Jackson and Berry find this ''price dispersion'' troubling, as it suggests that brokers use yield spread premiums as a device ''to extract unnecessary and excessive payments from unsuspecting borrowers'' (page 9).

Third, consider the confusion that the variety of loan products and permutations of those products can create. If informational asymmetries are significant, then lenders will be able to earn more when selling more complex products. The Urban Institute (2007b) reports that all borrowers see a benefit (in lower upfront cash costs) of only 20 cents for each dollar of yield-spread premium (actual or inferred) paid. Those who borrow through mortgage brokers see a benefit of only 7 cents per dollar, for a net loss of 93 cents on the dollar. Borrowers who simplify their mortgage shopping by rolling all lender/broker fees into the interest rate (i.e., get ''zero-cost'' loans) pay $1,200 less for their loans than brokers who pay lender or broker fees as measured by implicit YSPs. It appears that the industry is able to take advantage of loan complexity, which is evidence of price discrimination not related to the cost of originating the loan.

Fourth, consider other settlement charges. Title insurance is an industry with a strong potential for natural monopoly. The costs of title insurance are primarily related to research of property transactions. There is a large fixed cost of entry which is compiling a database of transaction and lending records. There should not be a great variation in settlement charges since the only component that does vary substantially is the insurance premium. The Urban Institute (2007b) finds an average $1,200 title charge in their sample of all loans with a standard deviation of $500. They also find a significant variation by state with New York, Texas, California, and New Jersey all costing at least $1,000 more than North Carolina, the lowest-cost state. A reasonable question is what extra benefits people in the high-cost states get relative to those in low cost states, or why costs are so high if there are no extra benefits. It is also useful to analyze total title costs on a state-by-state basis due to the different legal requirements that exist among the states and the different customs that might have evolved in them as well. HUD examined within state variation of settlement fees. One measure of variability that we calculated for each state was the difference between the median of the highest quartile of title charges and the median of the lowest quartile. This is a measure of the difference between the typical charge for the highest fourth of the borrowers and the lowest fourth of the borrowers within each state. This difference was over $1,000 for nine states. Due to the extent of price dispersion, we can expect significant savings from the proposed rule.

The primary purpose of this discussion was to show that there is great variation in closing costs and thus room for price discrimination. HUD would like to emphasize that the goal was not to portray lenders, and especially mortgage brokers, as unscrupulous and harmful to economic welfare. On the contrary, HUD recognizes that mortgage brokers and other lenders have played a crucial role in recent trends in home ownership. It is also clear from the statistical evidence presented in this section that there are many ethical lenders. One quarter of the borrowers in this sample paid no more than 2.4% in loan charges and 4.1% in total closing costs. Consider that if the entire market mirrored this more efficient segment, then RESPA reform would not be as urgent.

Appendix IV. Summary of Significant Issues Raised in Comments on the 2002 Initial Regulatory Flexibility Analysis

This section describes how HUD responded in this Initial Regulatory Flexibility Analysis (IRFA) to comments received on the 2002 IRFA. The primary comments on the 2002 IRFA included: a desire for more detailed information on the industries potentially affected by the rule and the expected effects of the rule on these industries on a per-firm basis, and more discussion of alternatives considered by HUD to minimize the impact of the rule on small business consistent while still achieving the stated objectives of the statute. The Office of Advocacy of the Small Business Administration, in particular, wanted to see more details on the industries and small businesses affected by RESPA reform.

Appendix IV.A. Detailed Industry Data and Analysis

Section Appendix V provides data on small businesses that may be affected by the rule and provides detailed breakdowns of the anticipated effects of the rule on all firms, small firms and very small firms. The analysis includes both industry total effects and per-firm effects. As explained in Section V below, Chapter 5 of the RIA provides extensive documentation of the characteristics of the industries directly affected by the rule, including various estimates of the numbers of small entities, reasons why various data elements are not reliable or unavailable, and descriptions of methodologies used to estimate (if possible) necessary data elements that were not readily available. The industries discussed in Chapter 5 of the EA included the following (with Chapter 5 section reference): mortgage brokers (Section II); lenders including commercial banks, thrifts, mortgage banks, credit unions (Section III); settlement and title services including direct title insurance carriers, title agents, escrow firms, and lawyers (Section IV); and other third-party settlement providers including appraisers, surveyors, pest inspectors, and credit bureaus (Section V); and real estate agents (Section VI).

Appendix IV.B. Alternatives Considered To Minimize Impact on Small Businesses

Section VI of the Appendix provides discussion of the alternatives considered by HUD in developing the proposed rule with a focus on those alternatives considered to minimize the impact on small business. Section VI includes summary discussion of the following major alternatives: Maintaining the status quo; not including the yield-spread premium calculation in the GFE; introducing the Settlement Services Package; offering packaging; and allowing dual packaging. Section VI also includes a discussion of steps HUD took to make the new GFE easier to implement for small businesses.

Appendix IV.C. Comments and Responses

Chapters 1–5 of the Regulatory Impact Analysis include detailed summaries of the comments submitted by small businesses and other firms on various aspects of the 2002 proposed rule and in response to the 2002 IRFA. Detailed discussion of comments received can be found in the preamble. Detailed analysis responding to comments received can be found in Sections VI and VIII of Chapter 3 of the RIA. Detailed discussion of comments related to the compliance burden of the rule can be found in Sections VII and VIII of this appendix. Analysis responding to some specific comments on the 2002 IRFA can be found in Chapter 3 of the RIA. Changes made to the 2002 proposed rule in response to comments received are summarized in Section VI of the Appendix.

Appendix V. Description and Estimate of the Number of Small Entities

Chapter 5 provides extensive documentation of the characteristics of the industries affected by the rule, including estimates of the numbers of small entities. The industries discussed in Chapter 5 included the following (with industry code and Chapter V section reference): mortgage brokers (Section II); lenders including commercial banks, thrifts, mortgage banks, credit unions (Section III); settlement and title services including direct title insurance carriers, title agents, escrow firms, and lawyers (Section IV); and other third-party settlement providers including appraisers, surveyors, pest inspectors, and credit bureaus (Section V); and real estate agents (Section VI). The specific industry names and industry codes (North American Industry Classification System, or NAICS code) for the mortgage originators and third-party firms covered in Chapter V are as follows:

Mortgage Origination Firms

1. Mortgage Loan Brokers (522310)
2. Commercial Banks (522110)
3. Savings Institutions (522120)
4. Real Estate Credit/Mortgage Bankers (522292)
5. Credit Unions (522130)

Third-Party Service Firms

1. Direct Title Insurance Carriers (524127)
2. Title Abstract and Settlement Offices (541191)
3. Offices of Lawyers (541110)
4. Other Activities Related to Real Estate (531390)
5. Offices of Real Estate Appraisers (531320)
6. Surveying and Mapping (except geophysical) Services (541370)
7. Credit Bureaus (561450)
8. Exterminating and Pest Control Services (561710)
9. Offices of Real Estate Agents and Brokers (531210)

Chapter 5 supports Chapters 3 and 6 by providing basic mortgage-related data on each industry and by explaining the various methodologies for estimating the share of industry revenue accounted by the different component industries and by small businesses within each component industry. Chapter 5 presents an overview of the industries involved in the origination and settlement of mortgage loans (see above list). Industry trends are briefly summarized and special issues related to RESPA are noted. There is also a description of the economic statistics for each industry, with an emphasis on each industry's share of small business activity. Both the estimation of the revenue share for various industry sub-sectors (e.g., large title insurers' share of total revenue in the title and settlement industry) and the estimation of the small business share of mortgage-related revenue within the industry, often involve several technical analyses that pull together data from a variety of sources, in addition to Census Bureau data. This leads to several sensitivity analyses to show the effects of alternative estimation methods and assumptions. This chapter also reports the revenue transfers from the RESPA rule for the specific industry sectors; these transfers are reported in dollar terms and, where possible, as a percentage of industry revenue. Finally, a number of technical issues and special topics, such as techniques for estimating the distribution of retail mortgage originations, are discussed. A technical appendix to Chapter 5 provides relevant definitions and explains the methodology associated with the economic data obtained from the Census Bureau. A data appendix in Chapter 5 includes tables with the economic data (number of firms, employment, revenue, etc.) for each industry sector.

Thus, the Regulatory Impact Analysis pulls together substantial data from the Bureau of the Census and industry sources to provide estimates of revenue transfers for different industries and for small businesses within those industries. Chapter 5 provides a full technical review of the data used and the various methodologies for estimating the small business share of industry revenues.

Drawing from the analysis in Chapters 3 and 5, Appendix A to this chapter provides estimates of the revenue impacts from the new GFE. These data are presented in aggregate form ($ million) and on a per firm basis, covering all firms (both employer and non-employer), small firms (small employer firms plus non-employer firms), and very small firms (very small employer firms plus non-employer firms). Separate data for non-employer firms are also provided. In some cases, different projections are provided for some of the more important sensitivity analyses conducted in Chapters 3 and 5. The technical analyses presented in Chapter 5 indicate some uncertainty around some of the numbers (such as the number of small mortgage banks, the split of revenue among different sectors of the broad title industry, etc.). Readers are referred to the technical discussion in Chapter 5 for various qualifications with the data and for various sensitivity analyses that illustrate the effects on the estimates of alternative assumptions. In addition, Chapter 5 explains the definitions of small and very small being used here.

Appendix VI. Alternatives Which Minimize Impact on Small Businesses

Under the Initial Regulatory Flexibility Analysis, HUD must discuss alternatives that minimize the economic impact on small entities consistent with the stated objectives of applicable statutes, including a statement of the factual, policy, and legal reasons for selecting the alternative adopted in the proposed rule and why each of the other significant alternatives to the rule considered by the agency was rejected. Many of the alternatives that HUD considered and implemented were directed at making the proposed GFE less burdensome for small businesses. These changes are described below. A more detailed discussion of the changes to make the GFE easier to implement for small businesses are provided in Section VIII of Chapter 3. For a discussion of all of the major alternatives considered to the proposed GFE, see Chapter 4.

This Regulatory Impact Analysis discusses several steps that HUD took that will assist small businesses involved in the mortgage origination and settlement process. Examples include simplifying the new GFE form (fewer numbers, etc.), designing the new GFE form so that there is a level playing field between lenders and brokers, and delaying the phase-out of today's GFE for twelve months. HUD also made numerous other changes that were designed to make the GFE easier to use, particularly for small businesses. These changes are discussed throughout Chapter 3 and summarized in several places in the Regulatory Impact Analysis. This section will list them again, as it is useful to provide a record of the changes made to the 2002 proposed rule that should make the new GFE easier to implement for small businesses. Considered as a group, these changes are important. While many are designed to address a problem faced by large as well as small lenders, for the most part, they address problems that would place a greater burden on small rather than large businesses.

Some examples of the changes that HUD made are the following:

- Clarifying that ''zero tolerance'' in the new GFE does not pertain in ''unforeseeable circumstances'' beyond the originator's control. This was in response to concerns expressed by lenders and brokers about their ability to control third-party costs and meet the specified tolerances in the 2002 proposed rule, the proposed rule. The tolerance for fees for lender-required, lender-selected third-party services was also increased from zero percent to 10 percent; further, tolerances no longer apply to items such as escrow expenses and government charges and fees. Relaxing tolerances benefit smaller firms, which would be more impacted by an underestimated fee.
- Clarifying the definition of ''unforeseen circumstances'' to include circumstances that could not be reasonably foreseen at the time of GFE application—examples include the need for a second appraisal or flood insurance.
- Changing the definition of an application so that it is consistent with the way consumers and lenders operate today—a ''GFE application'' would serve as a shopping application and a ''mortgage application'' would be submitted once a shopper chooses a particular lender, and would resemble the standard application in today's market and be the basis for full underwriting.
- Clarifying that only the ''mortgage application'' would be subject to Regulations B (ECOA) and C (HMDA), which is the current situation today.
- Reducing the period for the GFE tolerances to 10 business days, which gives borrowers ample time to shop and does not impose large operational and hedging costs on small lenders and brokers (as 30 days might have).
- Dropping the Annual Percentage Rate (APR) from the new GFE. Lenders and brokers objected to the requirement that they calculate the APR on the GFE; for a variety of reasons, HUD dropped the APR.
- Dropping the broker-lender split of fees from the GFE. Lenders and brokers disagreed with splitting out the broker and lender portions of the origination fee on the back page of the proposed GFE; HUD dropped that from the new GFE, as it was not useful for comparison shopping.
- Dropping the Title Agent/Title Insurance Premium Breakout. Title agents argued that breaking out the title insurance premium that goes to the underwriter from the rest of the title charges is costly and serves no useful purpose. This requirement has been eliminated, so there will be no compliance burden associated with the title agent/title insurance premium breakout on the GFE. The breakout was not useful for comparison shopping.
- Clarifying the ability to make cost adjustments as a result of information gained during the full underwriting process; and
- Allowing average cost pricing which will reduce the costs of keeping up with every ''nickel and dime'' of third-party costs.

The above changes address a number of practical and implementation problems raised by lenders, brokers, and others about the new GFE. They make these GFE form easier to use, particularly for small lenders and brokers.

Appendix VII. Compliance Costs and Regulatory Burden: New GFE

This section focuses on the compliance, regulatory, and other costs associated with implementing the proposed rule. It examines compliance and regulatory impacts of the new GFE on originators. There are two types of compliance and regulatory costs—one-time start-up costs and recurring costs. Section VII.B of the Appendix discusses start-up costs, noting that HUD has lengthened the phase-in period for the new GFE in order to reduce any implementation burden on the industry, particularly small firms. Section VII.C discusses recurring costs that are related to implementing the new GFE. The simplicity of the new GFE, plus the changes that HUD has made to improve the new GFE, will limit these annual costs, as discussed in Section VII.D. Section VII.E discusses compliance issues related to tolerances on settlement party costs. Finally, Section VII.F outlines efficiencies associated with the new GFE. Before examining the specific regulatory and compliance costs, Section III.A reviews the basic data used in estimating these costs. For a similar description of the costs on the settlement industry, see Section Appendix VIII.

Appendix VII.A. Data Used in Compliance Cost Estimates

The following tables provide a summary of the industry characteristics data used to develop compliance cost estimates for the GFE. Details on the derivation of these data are available in Chapter 5. The compliance costs of the GFE provisions of the rule apply mainly to retail loan originators. While wholesale lenders, for example, are involved in the mortgage origination process, they are not responsible for issuing the GFE—rather the originating lender or broker is responsible for the issuing the GFE to the borrower.[55] Therefore, data are presented only for those brokers and lenders that do retail mortgage loan originations. Settlement agents do not generate GFEs and therefore they would not be subject to these GFE-related costs. Settlement agents do, however, generate HUD–1s; since there are some changes to the HUD–1 form, there are compliance costs on settlement agents associated with that change. A major portion of the compliance cost will be the burden of performing the closing script accurately. Other third-party providers (e.g., appraisers) will face no compliance costs from the GFE provisions of the rule.

Chapter 5 of the RIA provides information on the total number of brokers and lenders that are likely to be affected by the new RESPA rule and its revised GFE form. Section II of that chapter explains that the number of brokers has grown substantially in recent years. In 2000, there were 30,000 brokers, but with the increase in refinancing, the number of brokers rose to 33,000 in 2001 and then jumped to 44,000 in 2002 and then to 53,000 in 2004. According to Census Bureau data, practically all brokers (99.1%) qualify as a small business. Thus, it is estimated that small broker firms have ranged from 32,703 to 52,523 over the past few years. As explained in Section III of Chapter 5, lenders that will be affected by the RESPA rule include: 7,402 commercial banks (4,426 or 59.8% are small), 1,279 thrift institutions (641 or 50.1% are small), 1,287 mortgage banks (1,077 or 83.7% are small), and 3,969 credit unions (3,097 or 78.0% are small).[56]

[55] If the wholesale lender generates the GFE, then there would be a charge to the originator (either a direct charge or a reduction in fees, compared with the case where the originator issues the GFE).

[56] See Section III.B.5 of Chapter 5 for issues related to the number of small mortgage banks. As also explained in that section, the credit unions are

Continued

Altogether, there are 13,937 lenders (including credit unions) affected by the RESPA rule, and 9,241 of these qualify as a small business.

Table A–4 provides the distribution of retail mortgage originations among the various industries and for small firms within each industry. Totals are estimated based on the number of mortgage originations (12,500,000 loans) that would occur in a ''normal'' year of mortgage originations (that is, not in a high-volume year with a refinancing boom). The data below assume that brokers account for 60% of mortgage originations and lenders, the remaining 40%.[57]

(See below for alternative origination volume and broker share estimates.)

TABLE A–4.—VOLUME OF RETAIL MORTGAGE ORIGINATIONS

Industry	All originations	Percent of originations	Originations by small firms	Percent industry originations by small firms
Mortgage Brokers	7,500,000	60.00	5,250,000	70.00
Commercial Banks	2,053,150	16.43	389,893	18.99
Thrifts	974,750	7.80	120,089	12.32
Mortgage Banks	1,551,500	12.41	644,803	41.56
Credit Unions	420,600	3.36	122,563	29.14
Total	12,500,000	100.00	6,527,349	52.22

As shown in Table A–4 it is estimated that 52% of mortgages are originated by small brokers and lenders.

Table A–5 provides the total number of workers and the number of workers in small firms engaged in retail mortgage origination by industry. It is based on the mortgage origination volumes depicted in Table A–4 and productivity rates of 20 loans per worker per year for mortgage brokers and lenders. See Section II.B.2.c of Chapter 5 for the derivation of the 20 loans per worker in the broker industry and see Section III.B.5.g of Chapter 5 for a discussion of the 20 loans per worker in the lender industry. Given the uncertainty around these estimates (and particularly the lender estimate which is obtained by simply assuming that lender workers are as productive as brokers), alternative estimates and sensitivity analyses are provided in Chapter 5.

As noted in Chapter 5, one alternative would be to choose a lower productivity number for lenders, which would be consistent with the widely held belief that brokers are more productive than lenders; in addition, it may be more appropriate to overestimate the number of lender employees affected by the RESPA rule than to underestimate them.[58] However, this analysis starts by assuming equal productivity for lenders and brokers.

TABLE A–5.—WORKERS ENGAGED IN RETAIL MORTGAGE LOAN ORIGINATION

Industry	Total workers	Workers in small firms	Percent of workers in small firms
Mortgage Brokers	375,000	288,750	77.00
Commercial Banks	102,658	19,495	18.99
Thrifts	48,738	6,004	12.32
Mortgage Banks	77,575	32,240	41.56
Credit Unions	21,030	6,128	29.14
Total	625,000	352,617	56.42

As shown in Table A–5, it is estimated there are 625,000 workers engaged in mortgage origination, with 352,617 of these operating in small businesses. As noted above, the mortgage volume figure (12,500,000 loans based on $2.4 trillion in originations) reflects industry projections of mortgage originations for 2008. Chapters 3, 4, and 5 conduct sensitivity analyses with a higher level of originations. For example, one could consider an environment where 15,500,000 loans were originated (compared with the 12,500,000 loans in the base case). In this case, the figures in Tables A–4 and A–5 would change. For example, the number of workers in the broker industry would increase to 438,038 (with 337,293 in small firms) and the number of workers in the combined lender group would increase to 271,250 (with 69,296 in small firms).[59] Below, sensitivity analyses cover these higher estimates of the number of workers affected by the RESPA rule.

Appendix VII.B. Compliance and Regulatory Burden: One-Time Costs

Several one-time compliance burdens can be identified that will result from the new rule. All involve the adjustment process from the old rule to the new rule. Although HUD received comments on the one-time compliance cost issues associated with the new GFE, commenters did not provide any useful data on the magnitude of these costs (see Section Appendix VII.B.5 below).

There are three major areas of expected one-time compliance costs of the new GFE. Those who generate the new GFE forms, loan originators, will need new software in order

the ones that report some mortgage origination activity.

[57] See Section III.B.5.d of Chapter 5 for the derivation of the distribution of retail originations among commercial banks, thrifts, and mortgage banks; the distribution used here is the ''adjusted distribution'' for the number of loans. See Chapter 5 for reasons why there is some uncertainty with the estimated distribution and for analysis of an alternative distribution.

[58] A comment should be made about the small business share for brokers. Section II.B.1 in Chapter 5 reports that small brokers account for 70% of broker industry revenue. Table A–4 assumes that small brokers account for the same percentage (70%) of the number of loans originated by all brokers; it is possible that this percentage could be too low, given that Section II.B.2.c of Chapter 5 derives an estimate of 77% for the share of industry workers in small broker firms. The 77% figure is used in Table A–5 (288,750 divided by 375,000) for estimating the share of workers in small broker firms. The small business share of the number of workers in each of the four lender industries in Table A–5 is assumed to be the same as in Table A–4 for the number of loans. See Section III.B.5 of Chapter 5 for the derivation of the small lender shares of lender originations.

[59] As explained in Chapter 5, this scenario assumes that the increase in mortgage originations comes mainly from brokers; the loans-per-worker assumption is increased to 23 for brokers (consistent with that number increasing in Olson's surveys during higher volume years) but kept at 20 for lenders since their volume does not increase much during this scenario.

to produce the new forms.[60] Their employees will need to be trained in the use of the new forms and software. Loan originators may seek legal advice to be certain that the arrangements they make to ensure that third-party service prices are accurate and within tolerances comply with the regulation. Loan originators may also seek legal advice regarding discount arrangements that are permissible under the new GFE. In this section, it is estimated that these one-time compliance costs will total $401 million, although it is recognized below that these costs could vary with several factors such as different levels of overall mortgage activity. Small brokers and small lenders firms will experience $280 million (or 70%) of these one-time compliance costs.

Appendix VII.B.1. Software Modification and Training Costs

Loan originators would need alterations to their software to accommodate the requirements of the new rule since they generate the new GFE. There would be one-time costs for production and installation of the new GFE (software development, etc.). Software modification, or new software, is needed because the GFE has been changed. The implementation of software varies with business size. Small originators are likely to use commercial off-the-shelf (COTS) software products while larger originators may produce their own software if in-house development is cheaper than buying from outside suppliers. HUD reviewed several software products for loan origination and closing advertised on the Internet.[61] Prices ranged from a flat $69[62] for one license to undisclosed negotiated prices based on the number of users and feature sets purchased. Software is generally priced according to the number of users (e.g., one license per user, or enterprise licenses based on the expected number of users in the enterprise).

One new requirement, implicit from the tolerances, is that originators will have to keep track of the costs listed on the GFE in order to ensure that the tolerances are not exceeded at settlement. Most of the software products HUD examined have the capability to access databases of information, including pricing information, of third-party service providers. Because these systems have the capability to access other databases, they would not need to be redesigned to carry forward prices from the GFE to the closing documents in order to determine if final settlement prices remain within tolerances. The GFE portion of the software would need to be modified to display the consolidated expense categories mandated in the rule. Redesigning the form appears to constitute a minor alteration of the software.

The new GFE also requires additional information. The first page summarizes worst case scenarios for the borrower: The maximum monthly interest rate, the maximum monthly mortgage payment, and maximum loan balance. Such information is obvious for most types of loans but could require more effort to calculate for more exotic loans such as a negative amortizing loan. Some loan origination software will already possess analytical capabilities. However, producers of less sophisticated programs will need to write a few additional lines of code to create the output for the first page of the new GFE. Nonetheless, the proposed rule would have no impact on the primary function of origination software and would require only minor changes.

Depending on the software that a firm has purchased there are three possibilities as to who pays the direct cost of developing new software. The first scenario is that a firm purchases an update of the program. This is a fairly standard option and is generally less than half the price of new software. Given that the changes required by the proposed rule are fairly minor, the price of an update should compensate software companies for the cost involved in altering their programs.

The second possibility is that a firm purchases new software, in which case the cost of redesigning the forms to comply with the proposed rule will be built into the purchase price. Firms that would purchase new software would include new entrants into the industry, pre-existing firms that would have bought new software for reasons unrelated to the proposed rule, and firms that use software for which updates are not offered. Many users routinely upgrade software as new versions are released and build the expected expenses into their business plans. To the extent that software is routinely upgraded, the extra costs of implementing the GFE changes will be reduced. In these cases, the software cost to the firm of the proposed rule is not the purchase price of the software but rather the increase in the purchase price as a result of the costs of redesigning software to meet RESPA guidelines.

A third scenario is that software companies are obliged or volunteer to offer free updates, in which the case the software cost of the proposed rule falls directly on software developers. However, indirectly, the cost of the new software will be shared by real estate and software firms. Software companies that offer free updates will price the risk of changes into the purchase price of the software. If a large unexpected change occurs, then the software company will bear the burden. However, the change required by RESPA will not be unexpected because the proposed rule will be made public and will not be costly for reasons previously discussed.

In all three scenarios, the cost of an update is a good approximation of the software cost of the rule. In the first scenario in which firms purchase an update, it would probably be an overestimate of the cost to a purchaser because an update may contain other useful improvements to the software. However, it is a reasonable estimate of the cost in that many firms would not purchase an update if not for the proposed rule. In the second scenario, in which a firm purchases new software, the price of an update could serve as an approximation of the cost of implementing the required changes and thus an estimate of the resulting increase in the price of new software. In the third scenario, where the software companies bear the direct cost of the change, the price of an update could serve as an estimate of the cost to software firms of producing free updates.[63]

In the first two scenarios, where firms bear the burden of the change in the software; the costs of new or updated software will depend upon the number of employees in the firm using the software. Virtually all software companies providing software to lenders for loan origination offer volume discounts. Such a pricing policy reduces the average cost for large firms. Second, in larger firms many employees will have specialized duties that do not include completing the new GFE form and so will not require updated software. Thus, it is likely that small firms will bear a greater per employee software cost from the proposed rule.

Based upon the discussion above and an examination of software pricing schemes, it is reasonable to make three assumptions in order to estimate the software costs of the proposed rule: (1) The cost per user is the cost of an update; (2) updates cost less than half of the cost of new software; (3) the costs per user for a firm decline significantly with the number of users. An example of the type of software that a firm might purchase is Bytepro Standard (by Byte Software, Inc., *http://www.bytesoftware.com*). This software has many analytical features such as the ability to calculate maximum loan amounts, which would be required by the new GFE. The software costs $395 for a two user package and $400 for five additional users. The per user cost for the first two is $198. The cost per user for an additional five is $80.

We can safely assume that the industry average of the cost of an update would be no more than $150 for the first user, $100 per user for the average small firm, and $50 for the average large firm.[64] Second, we assume that the proportion of workers involved in origination that use the software declines with the size of the firm. For small firms, we assume that three-quarters of all workers use the software and will need an update. For

[60] This analysis assumes that the mortgage broker, not the wholesale lender, produces the GFE in transactions involving mortgage brokers. To the extent that the wholesale lender is involved in producing the GFE the use of the broker data will result in an overestimation of the impact on small businesses (since small businesses make up a much larger portion of broker businesses than they do of wholesale lender businesses).

[61] Examples are: Vantage ILM, *http://www.vantageilm.com;* Utopia Originator from Utopia Mortgage Software, *http://www.callutopia.com/support.html;* The Mortgage OfficeTM from Applied Business Software, *http://www.themortgageoffice.com/main.asp;* and MORvision Loan Manager from Dynatek, *http://www.dynatek.com/products.asp.*

[62] Good Faith Settlement Software by Law Firm Software; *http://www.lawfirmsoftware.com/software/good-faith-estimate.htm.* Note that this is very basic software compared to other alternatives. More sophisticated software is more expensive.

[63] Correctly estimating the cost to software firms is difficult given the nature of the output. Development is a one-time fixed cost, whereas the cost of delivering software to one user is very low. Given the decreasing average costs, the aggregate economic impact to the software industry would depend upon the number of firms.

[64] Byte Software, Inc., offers an annual support service, which would include updates, for up to ten users for $300 per year. Every additional user over ten cost $30.

large firms, we assume that only half of the workers use origination software and need an update. Given these assumptions, the total cost to the industry of an update would be $33 million, of which $26 million is borne by small firms.[65] This amounts to an average software update cost of $83 per user.

In addition, each employee using the new software would require some time to adjust to the changes. The actual amount of time required to familiarize ones self with the new software is unknown. For this example it is assumed that 2 hours are required. If the opportunity cost of time is $72.12 per hour (based on a $150,000 fully-loaded annual salary), then the opportunity cost of software training would be $144 per worker using the new software. Software users often learn about new modifications without formal training by using them with very little loss of time or productivity. Thus the software training costs estimated below are likely an upper bound. Table A–6 shows the distribution of these costs by industry and the amount borne by small businesses within each industry. The table uses worker distributions from Table A–5 and assumes half of the workers in large firms and three-quarters of the workers in small firms use the software and will require upgrades and training. Given these assumptions the total software training cost is $58 million, of which $38 million is borne by small firms. The grand total for software upgrade and training cost is $91 million, of which $65 million is borne by small firms.

TABLE A–6.—ONE-TIME SOFTWARE UPGRADE AND TRAINING COSTS OF THE NEW GFE

Industry	Total software upgrade and training cost	Small business cost	Percentage small
Mortgage Brokers	$61,267,428	$52,891,226	86.3
Commercial Banks	11,647,288	3,570,897	30.7
Thrifts	5,249,891	1,099,855	21.0
Mortgage Banks	10,308,241	5,905,531	57.3
Credit Unions	2,569,710	1,122,511	43.7
Total	91,042,558	64,590,020	70.9

Alternative estimates could be made. If 4 hours (instead of 2 hours) of software training were required, then total costs would rise by $57 million to $148 million (with $103 million being the small business cost). Assuming that only two hours are required, but that the proportions of software users were raised to all of the workers in small firms and three-quarters of the workers in large firms, then the total software cost (including training) of the proposed rule would be $126 million, of which $86 million would be borne by small firms. If the proportions are increased (as in the latter scenario) and the hours are increased (as in the former scenario), then the total cost would be $206 million (with $137 million being the small business cost).

The estimates in Table A–6 above are based on a ''normal'' level of mortgage origination activity and not that of a high volume year which might occur as a result of low interest rates. High volume years bring with them increases in productivity by existing firms and employees (higher rates of loans per employee), new employees, and new entrants. New employees and new entrants would require additional software licenses even if there were no new rule changing the GFE. For this reason, basing the software upgrade compliance burden on a high volume year would overstate the burden. Using the higher rates of productivity associated with refinancing booms to compute software upgrade costs would tend to understate them. Therefore, use of the normal business volume probably provides the most appropriate estimate of this cost. Still, assuming a higher level of origination activity (15,500,000 loans) and a 65% market share for brokers, estimated software costs would be $118 million, and $86 million would be accounted for by small businesses (with one-half of employees at large firms and three-quarters of workers at small firms using the software and requiring 2 hours of training). As noted earlier, the costs of software upgrades required to implement the new GFE apply only to retail loan originators. These costs do not apply to wholesale lenders.

Appendix VII.B.2. Legal Consultation

Using the new GFE will entail a change in business practices, including making arrangements with third-party settlement service providers to ensure that prices charged will remain within the tolerances of the prices quoted. Loan originators will want to ensure that these arrangements do not violate RESPA. Loan originators may also seek legal advice regarding discount arrangements that are permissible under the new GFE. It is highly likely that the trade associations for the mortgage loan origination industries will produce model agreements or other guidance for members to help them comply with the new rule. Some originators may feel no further need for additional legal advice so that they would have no legal consultation expenses as a result of the rule. Larger originators may wish to seek a greater amount of legal advice, as they perceive themselves to be at greater risk of class action RESPA litigation.

The actual amount and cost of legal services that will be incurred because of the new GFE are unknown. While it is recognized that all firms might not seek legal advice, it would seem that many firms engaged in retail mortgage origination would want some minimal legal advice, so that they understand the new rules and regulations. If all 57,937 firms sought two hours of legal advice at $200 per hour, the fixed legal consultation expense would amount to $23 million. In addition, firms will seek further legal advice based on their volume of transactions; in this analysis, the total volume-based legal expense amounts to 4 times the fixed expense or $93 million. To show that this is a reasonable estimate, suppose a large originator, operating in all 50 states and the District of Columbia, required state-by-state legal reviews averaging 1-person-week (40 hours) per state. At $200 per hour, this would amount to $408,000. If all of the 100 largest originators acquired a similar amount of legal advice, the cost would come to $40.8 million, which leaves approximately $52 million for variable legal costs for other originators.[66] Under these estimates, total legal consultation expenses associated with the new GFE are expected to total $116 million and are distributed among industries and small businesses, which bear 60.3% of the legal cost, as depicted in Table A–7, which uses information on the distribution of firms and originations.

[65] To demonstrate that our estimate is a safe ceiling, suppose that there are one hundred software firms and that each one pays six programmers an average of $150,000 a year to upgrade the software to reflect the changes incurred by the proposed rule. The total cost to the software industry would be $90 million.

[66] If the per hour cost of legal consultation were greater than $200 per hour, then these estimates would rise proportionately with the increase in hourly legal costs.

TABLE A–7.—ONE-TIME LEGAL CONSULTATION COSTS OF THE NEW GFE

Industry	Total legal consultation cost	Small business cost	Percentage cost to small business
Mortgage Brokers	$73,219,520	$56,375,264	77.0
Commercial Banks	18,186,829	4,934,375	27.1
Thrifts	7,740,284	1,182,697	15.3
Mortgage Banks	12,020,625	5,212,708	43.4
Credit Unions	4,706,743	2,147,722	45.6
Total	115,874,000	69,852,767	60.3

The costs of legal consultation required to implement the new GFE apply only to retail loan originators. Wholesale lenders and settlement agents and other third-party settlement service providers do not provide GFEs and therefore they would not be subject to these costs.

Appendix VII.B.3. Employee Training on the New GFE

Loan originators must fill out the new GFE and be familiar with its requirements so that they can fill out the form correctly and respond to the borrower's questions about it. So, there would be a one-time expense of training loan originators' employees in the requirements of the new rule. While the actual extent of the required training is unknown, a reasonable starting point would be that one quarter of the workers in large firms and one half of the workers in small firms would require training concerning the implications of the proposed rule. We assume that small firms pay tuition of $250 per worker but that large firms receive a discount and pay only $125 per trainee. If the training lasts an entire day, then the opportunity cost of the time, at $72.12 an hour (based on a $150,000 fully-loaded annual salary) would be $577 per trainee. The total tuition cost to the industry would be $53 million and the opportunity cost of lost time would be $141 million, amounting to a total training cost of $194 million. The total one-time cost for RESPA training for originator staff in the new rule would come to $194 million or $310 per worker (averaged across all workers). The one-time cost for small businesses is $146 million. Table A–8 depicts the distribution of training costs among the retail mortgage origination industries and for small businesses in each industry. It uses data on workers from Table A–5.[67]

TABLE A–8.—ONE-TIME WORKER TRAINING COSTS OF THE NEW GFE

Industry	Total training cost	Small business cost	Percentage small business cost
Mortgage Brokers	$134,522,236	$119,387,019	88.7
Commercial banks	22,653,771	8,060,292	35.6
Thrifts	9,981,440	2,482,613	24.9
Mortgage Banks	21,285,461	13,330,070	62.6
Credit Unions	5,148,741	2,533,751	49.2
Total	193,591,648	145,793,746	75.3

As explained earlier, the costs of training are probably best estimated using the more normal mortgage environment, since many of the additional employees during a refinance wave are temporary employees who may either do only general office work that does not require any GFE-specific training or who may be trained on-the-job by existing permanent employees. Still, the higher figures are reported for those who believe they are the relevant figures.

The data and table presented above depict what is likely to be an upper bound for training costs. There are other, less costly ways in which the knowledge necessary to comply with the provisions of the final RESPA rule can be imparted to workers. Small firms, in particular, are likely to take advantage of information on complying with the final rule provided by trade associations and their business partners (such as wholesale lenders), and these firms may find the time and expense of formal training unnecessary. To the extent that this is the case, the estimates reported above will over state the impact on small businesses.

Appendix VII.B.4. One-Time Adjustment Costs

Comments. Loan originators commented that it would be costly to develop systems and train people in the new rule and the new systems. They commented that it would be especially costly to engage in two changes, the new GFE and GMPA, simultaneously. (Of course, the proposed rule only requires them to implement the new GFE.) Even worse, they said, would be to make both changes without the old GFE as an alternative. For example, the Consumer Mortgage Coalition (2002) commented that from a training, compliance and systems changes standpoint, HUD's proposals were of such a magnitude that they should be implemented in stages. The Mortgage Banking Association of America (2002) commented that the proposed changes to the GFE would impose operational difficulties and would serve to complicate the implementation of packaging. The MBAA stated:

The cost burden of requiring a lender to overhaul its operational and compliance infrastructure on a single level is always significant. Doubling this task—by introducing the revised GFE and the GMPA at the same time—will likely increase costs exponentially. Lenders have limited human resources in their technology departments. These resources are already taxed in updating systems caused by the proliferation of law and regulation changes on the local, state, and Federal levels. (p. 11)

Bank of America (2002) said that two years are needed to implement the new rule, stating:

[The rule] will require significant systems changes, possibly occupying full time all of the technical staff a mortgage loan originator has. It will also require changes to the way lenders price their loans. Extensive testing and training time will be needed. (p. 20)

[67] Sensitivity analysis shows the effects of changing the number of workers participating in the training. If one half (rather than one-quarter) of workers at large firms and three-fourths (rather than one-half) of the workers at small firms attended training, then the total costs would be $314 million (with the small business share being $219 million); the average cost per employee would be $503. However, as noted in the text, there may be other, less costly ways in which the knowledge necessary to comply with the GFE provisions of the final rule can be imparted to workers, which will reduce the number of workers that need formal training.

America's Community Bankers (2002) said there would be a ''host of compliance and operational difficulties'' with the proposed GFE. The American Bankers Association (2002) notes the following with respect to the GFE:

If the changes proposed by HUD, especially modification of the GFE, were to become final it would necessitate the banking industry's expenditure of extensive resources and time to become fully compliant. Banks would have to modify their mortgage origination policies and practices. They would have to retrain their employees involved in the mortgage process as well as those overseeing compliance with RESPA and Regulation Z. They would have to redesign their software programs to accommodate the changes incorporated in such a final regulation. (p.3)

America's Community Bankers, the Consumer Banker Association, and the Missouri Bankers Association wanted two years lead time to implement the proposed GFE.

Response. An important feature simplifying implementation of the proposed rule is that it does not allow for the MPO (or GMPA as it was called in the 2002 proposed rule). Another important feature simplifying implementation is a twelve-month period during which the new GFE could be used by an originator who wanted to make the switch, or the old GFE could be used as an alternative by one who is more reluctant. This allows those who want to use the new GFE to do so as soon as possible. At the other extreme, it allows others to wait up to twelve months to make the adjustment. Several points can be made about this option:

• Some might prefer to wait to see how the new GFE actually works in practice before deciding exactly how they want to proceed. With HUD's implementation schedule, they will have some time to see how others have fared.

• Some might want to see how borrowers have responded to the new loan origination option, thus increasing the likelihood of making the best choices for their firm when they implement the new GFE. The 12-month implementation schedule will allow time to observe borrower reactions.

• Some might want to see how other loan originators have coped with new arrangements with other settlement service providers. The implementation period will allow them some time to adopt those arrangements most likely to work for them.

• Some might want to see how competing software systems are serving various clients' needs, increasing the likelihood of picking the software system that would work best for them.

• Some might want simply to follow the lead of their wholesale lender or other lenders that they do business with. There will be some competitive pressure on wholesale lenders to develop products and systems that meet the needs of brokers and loan correspondents who provide them with their loans. The implementation period allows time for this to be worked out.

In short, there will be twelve months for those more eager to embrace the changes to be the guinea pigs for the transition. This should help ease the burden of adjustment for those who might find it most difficult to adjust quickly. One would also anticipate that information about the new GFE rules and about new software systems for handling the forms would be highly publicized through several means (industry conferences, seminars, advertisements, demonstrations, etc.).

Appendix VII.C. Compliance and Regulatory Burden: Recurring Costs

This section discusses recurring costs associated with the new GFE. Several topics are addressed, some of which have already been discussed in previous sections. It is estimated that the new GFE may impose recurring costs of $255 million per year but will probably be neutral (see the conclusion of Section VII.C.1). Costs of the additional time spent to arrange the pricing that protects the originator from the costs of the tolerances being exceeded is $300 million annually or $24 per loan (see Section VII.E.2). The potential recurring costs are thus $555 million annually or $44.40 per loan. The recurring cost on small business would amount to $290 million (52.2 percent of the total).

Appendix VII.C.1. Cost of Implementing the New GFE Form

This section examines the various costs associated with filling out and processing the new GFE. In their comments on the 2002 proposed rule, loan originators commented that the proposed GFE was longer than today's GFE and that it would take more time to fill out. In addition to settlement charges, the proposed GFE contained loan terms, a trade-off table, a breakout of lender and broker fees, and a breakout of title agent and insurance fees.

There are several aspects of the new GFE that must be considered when estimating the overall additional costs of implementing it. The following discusses the various factors that will reduce costs and possibly add costs to the GFE process. As is made clear by the discussion, there should not be much, if any, additional cost with implementing the new GFE (as compared with implementing today's GFE).

(1) *Disclosure of YSP.* Under the existing scheme, mortgage brokers are required to report yield spread premiums as ''paid outside of closing'' (POC) on today's GFE and HUD–1. Page 2 of the new GFE has a separate block for yield spread premiums (as well as for discount points). In order to fill out a GFE under the proposed rule (as well under the 2002 proposed rule), the mortgage broker must have a loan in mind for which the borrower qualifies from the information available to the originator. Pricing information is readily available to mortgage brokers, so there is no additional cost incurred in determining the yield spread premium or discount points since they have to look and see if there is a yield spread premium under the current regime anyway. Since it is reasonable to assume that all brokers consult their rate sheets prior to making offers to borrowers, it is reasonable to assume that they know the difference between the wholesale price and par. It does not appear that disclosing the yield spread premium or discount points adds any new burden.

(2) *Itemization of Fees.* The reduction in the itemization of fees will lead to fewer unrecognizable terms on the new GFE.[68] That should lead to fewer questions about them and less time spent answering those questions. Of course, to the extent that the originator is precluded from including junk fees on the GFE, he or she will not have to spend any time trying to explain what they are. The confusion avoided may lead the borrower to better understand what is being presented so that questions on useful topics are more likely to come up and the originator can spend his time giving useful answers (or more time will be spent explaining useful things). In all, the simpler GFE produces a savings in time for originators and borrowers.[69]

(3) *Summary Page.* A summary page has been added to the new GFE in the proposed rule. But it should be noted that Sections I and II (on the summary page of the new GFE) ask for basic information (e.g., note rate, loan amount) that is readily available to the originator and thus do not involve additional costs. The summary page simply moves items around or repeats items rather than requiring new work.

(4) *Trade-Off Table.* There is a burden to producing and explaining the worksheet in Section IV (on page 3 of the GFE) showing the alternative interest rate and upfront fee combinations (the so-called ''trade-off'' table or worksheet). Many commenters said customizing the trade-off table with the individual applicant's actual loan information would be difficult; these commenters recommended a generic example, possibly placing it in the HUD Settlement Booklet, rather than providing it with the GFE. However, it is important to remember that the information in the worksheet is likely to be a reflection of a worksheet the originator already uses to explain the interest rate/upfront fee trade-off. While there may be a burden to explaining how the interest rate-point trade-off works, this explanation is something all conscientious originators are already doing in the origination process. In today's market, most lenders and brokers likely go over alternative interest-rate-point combinations with potential borrowers. For these originators, there is no additional explanation burden arising from the production of this worksheet. To the extent that some lenders only explain one option to a particular borrower (even though they offer others), there would be some additional costs

[68] The fees in the lender-required and selected services section will still be itemized (e.g., appraisal, credit report, flood certificate, or tax service) as will those in the lender-required and borrower selected section (e.g., survey or pest inspection). There will, however, be no itemization or long lists of various sub-tasks of lender fees or title fees, often referred to as junk fees.

[69] Several items were dropped from the new GFE, as compared with the proposed GFE: the APR, the breakout of the origination fee into its broker and lender components, and the breakout of the title services fee were dropped. These were considered unnecessary for comparison shopping.

for those lenders. Today, most originators present to borrowers much more complicated sets of alternative products than captured by the worksheet. It is important to remember that the main purpose of the worksheet is simply to sensitize the borrower to the fact that alternative combinations of interest rates and closing costs are available.

With respect to customizing the worksheet to the applicant's actual offer, the information on the applicant's loan is already on the new GFE, so that would not appear to be a significant problem, as that applicant information can be linked directly into the worksheet. Then, there is the issue of the two alternative combinations, one with a lower interest rate and one with a higher interest rate. Most originators offer loans with several interest rate and point combinations from which the borrower chooses. As noted above, they probably have already discussed these alternative combinations with the applicant. The originator would pick two alternatives from among the options available but not chosen by the borrower when he picked the interest rate and point combination for which his GFE is filled out. The originator would have to punch these other two combinations into his GFE software (two interest rate and point combinations) in order for the software to fill out the form. In the event that the originator does not use software to make these calculations, they would have to be done by hand.

(5) *Costs of Re-Disclosing the New GFE.* As discussed in Chapter 3, if the borrower does not qualify for the loan presented in the originator's GFE and a new loan is offered, a new GFE must be filled out with the appropriate changes. In addition, if there are unforeseen circumstances or changes requested by the borrower, a new GFE must be issued with the appropriate changes. But the borrower would be given these changes today for a new loan (but a new GFE would not be issued). The rule simply requires that the new information be conveyed to the borrower through a new revised GFE. For further information, see the discussion of re-disclosure costs below in Section VII.D.2.

(6) *Documentation Costs.* Loan originators are required to document the reasons for changes in any GFE when a borrower is rejected or when there are unforeseeable circumstances that result in cost increases. Once a GFE has been given, there are several potential outcomes. One is that the loan goes through to closing with tolerances and other requirements met. Another is the borrower terminates the application. Borrowers could also request changes, such as an increase in the loan amount. There could also be a rejection, a counteroffer, or unforeseen circumstances.

The first two require no special treatment. Borrower requested changes do not require documentation but do require a new GFE, as explained in (5) above. The case of borrower rejection (which assumes there is no counteroffer accepted by the borrower) requires documentation today under the Equal Credit Opportunity Act (ECOA). Under ECOA, the originator must document the reason for a rejection and retain the records for 25 months, which is also the requirement in the proposed rule. Therefore, there is no additional documentation required in case of a rejection. There is no documentation requirement for a counteroffer, but the lender must issue a new GFE to the borrower; the minimal burden associated with issuing an additional GSE as discussed in Section VII.D.2 below.

Documentation for unforeseeable circumstances adds a new requirement. The additional burden associated with unforeseen circumstances comes from having to document the reasons for the increase in costs and from determining that the amounts of the increases in charges to the borrower are no more than the increases in costs incurred by the unforeseeable circumstances. The Department does not require that a justification document be prepared. Since there are no special reporting requirements when unforeseeable circumstances occur, compliance could be met by simply retaining the documentation in a case binder, as any other relevant loan information might be retained in a case binder today. For example, itemized receipts for the increased charges would simply be put in the loan case binder (as they probably are today). Case binders are stored now. The additional cost of identifying and storing the documentation in that binder would be de minimus. This would represent little burden on the originator, particularly since unforeseen circumstances will not be the norm.

There may be some record retention issues with small originators, such as brokers. If small originators retain case binders today, then their situation would be similar to other originators. If they do not retain the case binder today, then they may choose to do so, or they may rely on their wholesalers for record retention. It might well become a selling point for wholesalers. Relative costs of storage, reliability, and accessibility would determine who could best perform this function.

(7) *Crosswalk from New GFE to New HUD–1.* The HUD–1 has been changed so that it matches up with the categories on the new GFE—making it simple for the borrower to compare his or her new GFE with the final HUD–1 at closing. In addition, a closing script has been added so that the settlement agent is required to explain the crosswalk. The simplification of the GFE does not add any burden for the borrower to the comparison of the figures on the two forms—rather it will be reduced since it will now be easier for the borrower to match the numbers from the GFE (issued at time of shopping) with those on the HUD–1 (issued at closing). Compared with today, it also eliminates the step of adding a pointless list of component originator charges to get the relevant figure, the total origination charge. In addition, the elimination of junk fees on the GFE may lead to the elimination of them on the HUD–1 since they may have been on the GFE only to overwhelm the comparison shopper. Even without the script, the settlement would have been more transparent for the borrower. However, requiring that a script be completed by the settlement agent and read to the borrower will impose some costs on the settlement agent. Compliance costs of the script are discussed in detail in Section VII.C.2 below.

(8) *Mortgage Comparison Chart.* The Mortgage Comparison Chart is the fourth page of the GFE. It is delivered to the borrower as a blank form. The borrower is free to fill it out and use it to compare different loan offers. The loan originator or packager is only required to hand it out, but has the option of answering borrower questions about it. The short, simple, and self-explanatory nature of the form leads the Department to believe that the additional costs per form, if any, borne by an originator or packager would approach zero.

Summary. To summarize, the discussion of the above factors identifies offsetting costs and suggests that there will be little if any additional annual costs associated with the new GFE. Practically all of the information required on the new GFE is readily available to originators, suggesting no additional costs. The fact that there are fewer numbers and less itemization of individual fees suggests reduced costs. The fact that the GFE figures are displayed on the HUD–1 will substantially simplify the closing process. In addition, Section D below lists further changes that HUD made to the form that are likely to reduce costs. On the other hand, there could be some small amount of additional costs associated with the trade-off table and documentation requirements. If there were additional costs of, for example, 10 minutes per GFE, the dollar costs would total $255 million per year.[70] [71] But given the above discussion of offsetting effects and the improvements made to the form, there are likely to be no additional net costs with implementing the new GFE. Note, however, that there is the potential for recurring costs from the script required at closing. This issue is summarized in Section VIII.

[70] This calculation assumes a $150,000 fully-loaded annual salary; dividing by 2,080 hours yields $72 per hour, or $12 for ten minutes. Assuming 21,250,000 applications, produces a cost figure of $255 million. At 15 minutes, the cost estimate would rise to about $382.5 million. In the higher volume environment (26,350,000 applications), the overall cost figure would be $316.2 million if the per application cost was $12 for ten minutes.

[71] We have used a fully-loaded hourly opportunity cost of $72.12 for highly-skilled professional labor throughout the Economic Analysis. For many functions as well as locations this amount is probably an overestimate of the hourly opportunity cost. However, our goal in the Economic Analysis is to accurately measure the upper bound of the costs of the rule. An alternative method would be to generate an estimate of the average variable cost from industry-specific data. For example, in Tucson, Arizona, the average unit labor cost (salary, bonuses, time off, social-security, disability, healthcare, 401(k), and other benefits) is $30.73 per hour for loan officers ($23.97 for a Loan Officer/Counselor; $28.48 for a Consumer Loan Officer I; and $39.75 for a Consumer Loan Officer II). Additional costs to be considered are rent ($2812.50 per month for 1500 square feet) and computer equipment ($560 per month). Summing this gives us an hourly cost of $31.14. An additional ten minutes per closing would increase costs by $5.19 per loan. The estimate of the recurring annual burden of the new GFE could reasonably be assumed to be $110 million, much less than the $255 million used throughout this analysis.

Appendix VII.C.2. Crosswalk Between the GFE to the HUD–1

The following paragraphs describe HUD's response to comments from the 2002 proposed rule on the crosswalk between the GFE and HUD–1 as well as a description of the development of the crosswalk. The compliance costs of the crosswalk are described in Section VIII.

Comment. Many commented that borrowers would require more help in comparing the proposed GFE to their HUD–1. The HUD–1 may contain all of the detail it has today while the GFE shows subtotals for major categories of settlement costs.

Response. While the forms do not match-up fee-for-fee, they do not have to match-up that way today under the GFE. In the area of lender fees on the GFE under today's rules, there would typically be several itemized fees (e.g., application fee, underwriting fee, etc.) despite the fact that they all go to the originator. Thus, the borrower would have to make several GFE-versus-HUD–1 comparisons of lender fees that do not have to match up dollar-for-dollar. Under the new rule, the borrower would add up the lender fees (which would typically be in the 800 series on the HUD–1) and look for that one number, ''Our Service Charge,'' on the new GFE. This would be no more difficult than before.

The HUD–1 has been changed so that it matches up with the categories on the new GFE—making it simple for the borrower to compare his or her new GFE with the final HUD–1 at closing. The GFE has been standardized and the titles of sections in the HUD–1 have been renamed to match with the GFE. Numbered references to the lines in the GFE are included in the HUD–1 to make it easier to match the appropriate lines. Finally, a crosswalk between the GFE and the HUD–1 has been added to the HUD–1 as an addendum. The settlement agent will be required to read the script to the borrower and guide him or her through the comparison of the GFE and the HUD–1 forms.

It should be noted, however, that even without the script, the borrowers might require less help in comparing GFEs to HUD–1s under the new rule. There is only one space for originator fees on the GFE. Originators who might otherwise break up their fee into a large number of components to overwhelm borrowers do not have that option on the new GFE. Borrowers will make their choices based on the GFE that has only one originator fee. Once the borrower is committed, originators might decide there is no advantage to splitting this figure into a large number of components since delivering overwhelming detail designed to affect the choice of loans after the choice has been made is pointless. If so, they would report only one originator fee on the HUD–1. If borrowers have only one originator fee on the HUD–1 and it matches the only originator fee on the GFE, then borrowers will require less help in comparing the originator's fees on the two documents.

In the area of title services, today the lender might estimate this cost with one number or an array. But if the originator does not initially know who will perform this service, the figures on the HUD–1 in the end could bear little semblance to those on the GFE. Under the new rule, title services, owner's title insurance, and borrower's title insurance are shown. The latter two will be itemized in the 1100 series and title services will be the sum of the rest of the numbers in the 1100 series of the HUD–1. Adding up the figures in the 1100 series and subtracting out the owner's title insurance premium (which is not covered by the 10% tolerance) is simple arithmetic. Adding that sum to the other third-party fees is more addition. Seeing if the total of these third-party fees is ten percent over the estimates involves one comparison. The new rule changes the procedure from making numerous charge-by-charge comparisons, for which matching entries may be missing on either form, to an exercise in adding first and then making a few comparisons. It is not clear that the new rule involves more difficulty or time than the old rule for a borrower who wants to compare the GFE to the HUD–1. It may well be easier for borrowers to compare GFEs to HUD–1s under the new rule than it was under the old. In addition, the required script will provide a standard explanation of the crosswalk.

The crosswalk tested by the Kleimann Communication Group met with mixed results. The crosswalk was tested in rounds two and three of the consumer testing of the forms. The conditions tested in round three were different than in round two since the form and tolerance scheme had changed. The first two numbers on page 2 of the round two GFE were dropped and the form began with what had been the adjusted origination charge. Also, the tolerances had changed from an individual zero tolerance for the fees of originator selected third-party providers and an individual ten percent tolerance for third-party providers where the borrower used a referral made by the originator, to an overall ten percent tolerance on originator and third-party fees so long as the borrower selected providers had been a referral from the originator. Also, the tolerance was dropped on reserves or escrow.

The crosswalk was tested as a stand-alone document; the subjects got no help at all from the testers. No verbal instructions were given and no questions of substance were answered. Under these circumstances, the subjects had a wide range of success rates in filling out the crosswalk. In the ordinary course of a closing, however, the borrower could be accompanied by a spouse, friend, or real estate agent who might help the borrower figure the crosswalk out. There is also the settlement agent who is likely to be an expert in this field, would understand the crosswalk, and could answer questions the borrower had about comparing charges on their GFE and HUD–1, i.e, performing the crosswalk. The crosswalk is likely to work much better in practice than it did in the isolation of stand-alone testing.

The proposed rule provisions for describing loan terms in the new GFE and the HUD–1 closing script are somewhat duplicative of the Truth in Lending Act (TILA) regulations, however the differences in approach between the TILA regulations and HUD's proposed RESPA rule make the duplication less than complete. The TILA and RESPA approaches to mortgage loan terms disclosure are most similar when the loans are very simple, e.g., fixed interest rate, fixed payment loans. The approach differs for more complex loan products with variable terms. In general, TILA describes how variable terms can vary (e.g., the interest rate or index to which variable interest rates are tied, how frequently they can adjust, and what are the maximum adjustment amounts, if any), but forecasts the ''likely'' outcome based on an indefinite continuation of current market conditions (e.g., the note rate will be x in the future based in the index value y as of today). The RESPA disclosures in the GFE and HUD–1 closing script focus the borrower on the ''worst case scenario'' for the loan product to ensure borrowers are fully cognizant of the potential risks they face in agreeing to the loan terms. The disclosures on the GFE are meant to be as simple and direct as possible to communicate differences among loan products. HUD's approach to these disclosures thus supports consumers ability to shop for loans among different originators. For a given set of front-end loan terms (initial interest rate, initial monthly payment, and up-front fees), originators have an incentive to offer borrowers loans with worse back-end terms (e.g., higher maximum interest rate, higher prepayment penalty) to the extent capital markets are willing to pay more for loans with such terms. While brokers are required to disclose such differentials on the GFE and HUD–1, lenders are not. HUD's proposed GFE will help consumers to quickly and easily identify and distinguish loan offers with similar front-end terms, but worse back-end terms, while shopping for the best loan. Requiring a script will act to double-check the HUD–1 and thus enhance the realization of the benefits of the simpler GFE.

Appendix VII.C.3. Multiple Preliminary Underwritings

Comment. Every application under the new rule requires preliminary underwriting. Since borrowers who shop may seek out multiple GFEs, there will be multiple underwritings. Commenters said this will add to the underwriting burden firms incur today.

Response. Every application under the 2002 proposed rule that generates a GFE will require preliminary underwriting in order to come up with an early offer for the borrower. Originators can charge a fee for issuing a new GFE. It is hoped that the charge for this, if any, would be small enough so that it is not a significant deterrent to effective shopping. But whether or not there is a charge, there are real resource costs associated with preliminary underwriting. The additional cost generated depends on the number of applicants and the number of GFEs they get. Since every completed loan eventually gets underwritten in full, the additional cost of preliminary underwriting depends mainly on the number of additional times that preliminary underwriting occurs beyond the one associated with the full underwriting that would have occurred under the existing scheme. It cannot be determined how many additional GFEs the average borrower would get under the new rule. Borrowers might continue the informal shopping method that many use today—gathering information and making inquiries to lenders and brokers about their products and their rates, even before deciding to proceed with the request for a more formal quote using the GFE. In other words, they may formally apply only after deciding who offers the best terms. The simple format and clarity of the new GFE form will enhance this informal information gathering process; in fact, the increased efficiency of informal shopping (calling around, checking web sites, etc.) could be an important benefit of the new GFE. Since shoppers as well as originators will be familiar with the GFE, these forms will likely serve as a guide for practically any conversation between a shopper and an originator, or for any initial request by a shopper for preliminary information about rates, points, and fees. For these borrowers, the new GFE simply pins down the numbers. Others, on the other hand, may obtain multiple GFEs and use them to shop.

There are currently 1.7 times as many applications as loans originated; therefore, if originations are 12.5 million, full underwriting is started (and probably completed) for about 21.25 million applications, including 8.75 million (21.25 million minus 12.5 million originations) that are not originated. Under the proposed rule, preliminary underwriting should decrease the number of applications that go to full underwriting (e.g., an applicant may be denied during the preliminary without having been charged for an appraisal); that is, some of the 8.75 million that are not originated may be disapproved at the preliminary stage rather than going through full underwriting (as they might today). This savings in appraisal, verification, and other incremental underwriting costs that are avoided would tend to offset the increase in cost resulting from the extra preliminary underwriting noted in the above paragraph. However, it is difficult to estimate these effects.

Appendix VII.D. Changes in the Proposed Rule That Reduce Regulatory Burden [72]

The proposed rule contains several changes from the 2002 proposed rule that are designed to reduce regulatory burden.

Appendix VII.D.1 Items Dropped From the Proposed GFE

Several items that commenters were concerned about are not included on the final GFE:

Lender/Broker Breakout. Loan originators argued that breaking out the origination charges into its broker and lender components is costly and serves no useful purpose. This requirement has been eliminated so there will be no compliance burden associated with the lender/broker breakout on the GFE.

Title Agent/Title Insurance Premium Breakout. Title agents argued that breaking out the title insurance premium that goes to the underwriter from the rest of the title charges is costly and serves no useful purpose. This requirement has been eliminated, so there will be no compliance burden associated with the title agent/title insurance premium breakout on the GFE.

APR. Loan originators commented that including the APR on the GFE was an unnecessary burden since it is duplicated on the TILA forms. There will be no compliance burden with the APR since that term has been dropped from the GFE.

Appendix VII.D.2 Cost of Re-Disclosure

Comment. Loan originators commented that re-disclosure would be costly. Under the 2002 proposed rule, a new GFE was to be filled out if the borrower did not qualify for the loan presented to him or her on the original GFE or if the borrower requested a change in the loan that would invalidate the original GFE. The GFE in the proposed rule has similar requirements. For example, the appraisal might come in lower than the value stated by the borrower and result in the need for mortgage insurance or a change in the mortgage insurance rate. Or, the borrower might request a change in loan product, interest rate, or loan amount. These situations would require a new GFE.

Response. If the borrower does not qualify for the loan presented in the originator's GFE and a new loan is offered, a new GFE must be filled out with the appropriate changes. If a borrower did not qualify for the loan under the old rule, no new GFE would be required, but the borrower would be told of the changes in the loan program and changes in fees that would result. The proposed rule (as well as the 2002 proposed rule) requires that the new information be conveyed to the borrower through a new revised GFE rather than through some other medium.

The only change is the method of communication. The data and other information on the counteroffer are readily available to the originator. In addition, one who receives a counteroffer must be made aware of the changes in the loan terms in order to properly prepare for the closing. For example, the borrower would have to know the new settlement costs in order to show up at settlement with a check for the right amount. So, counteroffer information is certainly already being conveyed today under existing rules. There would seem to be little cost in the change to require this information to be conveyed in a new GFE. If it took 10 extra minutes per new GFE over and above the time spent today conveying the information for the new offer, that would come to $12 extra cost per form. But there would be offsetting decreases in costs as well. There would be a decrease in confusion at the settlement table that would result from the borrower having a ''correct'' GFE for the offer accepted rather than the irrelevant GFE for the loan for which the applicant did not qualify. Any attempt to reconcile the old GFE with the HUD–1 would be confusing and ultimately unsuccessful. The new GFE, of course, could be reconciled with the HUD–1. The value of the time saved from being able to match the correct GFE with the HUD–1 should far exceed any additional cost resulting from the requirement that the new offer cost estimates must be conveyed in the form of a new GFE.

Appendix VII.D.3 Increase in HOEPA Loans

Comment. Loan originators commented that the reporting requirements for the yield spread premium would increase the fees reported by brokers and increase the number of loans subject to HOEPA regulations. As a result, HOEPA compliance costs will be incurred on a larger number of loans.

Response. The will be no compliance burden associated with increased HOEPA coverage since there will be no increase in HOEPA coverage. The comment assumes that the finance charge used to calculate the APR in the future would include the service charge rather than the adjusted origination charge that is the equivalent of what is reported under current rules. If it were true that the service charge was to be used under the new rule, the finance charge and APR would rise leading to more HOEPA loans and more HOEPA compliance burden. The Federal Reserve, however, will require the adjusted origination charge, equivalent to what is required today, to be used in calculating the finance charge and APR under the new rule. Consequently, there will be no RESPA mandated change to the calculation of the finance charge or APR on loans originated under the new GFE, and, therefore, no resulting increase in HOEPA compliance burden for loans originated under the new GFE.

Appendix VII.D.4 Treatment of Government Fees and Reserves/Escrow

Comment. Loan originators argued that these tolerances (zero on government fees and 10 percent on escrow) imposed burdens on them that were unnecessary. Escrow deposits can be difficult to determine within three days, especially when the property is new construction. These are not retained by the lender but are held on behalf of the borrower and are covered by the escrow rule. As with the other tolerances, small firms commented that they would be at a disadvantage relative to their large counterparts from the risks associated with having to cover any charges in excess of the tolerances.

Response: In the proposed rule, there will be no compliance costs resulting from tolerances on escrow since this tolerance protection has been eliminated. The zero tolerance on government recording fees and transfer taxes remains.

Appendix VII.D.5 Required Time for the GFE To Be Open to the Borrower

Comment. Loan originators argued that 30 days was too long for a GFE to be binding. In that time, some prices could change and the originator would have to bear the price increases that resulted.

Response. The time period for which the GFE will be open has been reduced from 30 days to 10 business days. It is unlikely that there would be any changes in that short a time that would be unanticipated and lead to the loan originator having to cover any charge in excess of the tolerances.

Appendix VII.D.6. Earlier Triggers for HMDA and Fair Credit

Comment. The new definition of application in the 2002 proposed rule was

[72] See Chapter 3 for a more detailed treatment of changes listed in this section.

designed to get the borrower good shopping information earlier in the application than under the current scheme. Loan originators complained that the new definition would trigger more GFEs than it had before. It would also trigger more Truth in Lending Forms as well as more Regulation B and C (HMDA and Fair Credit) reporting requirements for applicants who were at an earlier stage in the process than before. This would generate additional compliance burden as a result of having to generate more of these forms.

Response. As discussed in Section VI of Chapter 3 of the RIA, the definition of application has been bifurcated. The definition of ''application'' for GFE and TILA purposes will remain as in the 2002 proposed rule and result in earlier delivery of these forms while the definition for Regulations B and C purposes will be met when the borrower completes the application process by selecting a loan originator with whom his application will go forward. There will be no increase in reporting burdens because the timing requirements have not changed under the proposed rule.

Appendix VII.E. Other Compliance Costs: New GFE

This section discusses compliance issues related to the zero tolerances on lender fees (Section III.E.1) and the 10% tolerance on third-party fees (Section III.E.2).

Appendix VII.E.1. Zero Tolerances on Lender Fees

Comment. Originators commented that the zero tolerance on lender fees makes it difficult to switch borrowers from one loan to another if the fees are different. Such switching can be in the borrower's best interest. In such cases, the originator could keep the same GFE and possibly earn less on the loan, or have to fill out a new GFE for the borrower. The commenters said either alternative is costly to the originator.

Small originators commented that zero tolerance puts a greater burden on them than on larger originators. Their smaller number of transactions gives them a smaller base over which things can average out. One particular loan that turned out to be much more costly than estimated would have a larger proportionate negative effect on a small firm than on a larger counterpart that could average this out over a much larger number of transactions.

Response. This feature of the proposed GFE remains. The Department believes that it is not difficult for a loan originator to figure out its own price for its own product in three days. If the borrower does not qualify for the loan product described in the GFE and is rejected for that loan, the originator may offer the borrower another loan for which he may qualify and present the borrower with a new GFE for that loan. If the fees are higher for the new product, the GFE may reflect those higher fees and the originator is not limited to the lower fees of the original loan product.

Appendix VII.E.2 Tolerances on Third-Party Fees

The GFE tolerance requirements in the new rule require loan originators to bear the full burden of any third-party charges that exceed the limits set by the tolerances. Paying the excess to borrowers or incurring the costs to ensure that the third-party fees fall within the tolerances is a compliance burden.

Under the 2002 proposed rule, zero tolerance applied to fees for third-party services that are required by and selected by the lender. A ten percent tolerance applied to the required third-party services where the borrower chooses a firm referred by the originator.

No tolerance applied to third-party fees where the borrower chose a provider without a referral from the originator. The rational for the zero tolerance was that a loan originator should know the price of a service if it required the use of its chosen provider. In the case of making referrals, the loan originator could be expected to have some knowledge of the market. In fact, it should have some knowledge if it is to meet even the weakest concept of ''good faith.'' The 10 percent tolerance seemed like a reasonable limit for price dispersion for services obtained in a market that could be competitive if the buyers had good information. It is also simple for borrowers quickly to compute 10 percent of the total fee and determine if final charges are within the tolerance. In order to protect themselves from charges in excess of the limits set by the tolerances, originators would have to gather price information in the market and possibly set up agreements with some third-party providers to perform settlement services at prearranged prices. Those originators who would have gathered more information than they do today or made more pricing arrangements than they do today would have incurred an increase in regulatory burden resulting from the new rule.

Comment. Loan originators wrote that they should not be required to pay the bills for third-party fees in excess of the tolerances since they do not control those fees. They argued that their expertise is as originators, not as appraisers or title companies. They claimed that they do not know who will perform all these services at application, so the price is indeterminate. In addition, there are occasions when services beyond the normal minimum will be required, but that cannot be known at application. For example, additional appraisal work may be required or some work may have to be done to clear up a title problem. So prices and even some services that end up as being required are unknown at application.

Small originators made the same argument that they made on the zero tolerance for lender fees. They will be at a disadvantage if they have to cover the third-party fees in excess of the tolerances since they have a smaller base on which to average out these excess fees. If the loan originator solves its problem by using only those third-parties that agree to fixed prices, that shifts the burden to the third-party. Small third-party providers made the same argument that small originators made. They then will be disadvantaged relative to large third-party providers by having to bear the risk of the unpredictable cost that cannot be averaged out over a large number of transactions.

Response. The tolerance scheme for third-party services has been changed in the proposed rule. An overall tolerance of ten percent now applies to the sum of (a) third-party fees for services where the originator requires the use of a specific provider or (b) third-party fees where the borrower uses a provider whose name was given to him by the originator in response to a request for a referral.[73] As mentioned above, the 2002 proposed rule had a zero tolerance on (a) and a 10 percent tolerance on (b). The sum of the fees on the HUD–1 for third-party providers selected by the originator or used as a result of the referral process cannot exceed the sum of these fees on the new GFE by more than 10 percent. As in the 2002 proposed rule, no tolerance applies where the borrower elects to use a provider without the referral from the originator.

Tolerances will impose some burden on originators. Since the protection of tolerances kicks in only if the originator requires the use of a particular provider or if the borrower comes to the originator and asks where the services may be purchased within the tolerances, the originator must have reliable third-party settlement service provider pricing information or risk paying the charge in excess of the tolerance. Some originators might simply check out the market prices for third-party services from time to time, formulate estimates such that several of the prices charged by the third parties fall within the tolerance, and trust that nobody to whom they refer the borrower charges a price in excess of the tolerance.[74] Other originators might want more protection and have contracts or business arrangements in place that have set prices for services that are not in excess of the tolerances.

Either case requires the originator to do more than today, although even today originators fill out GFEs with estimates for third-party settlement services. In the first case, the liability in the event a tolerance is exceeded would lead to at least a little more work gathering information prior to filling out the GFE. In the second case, more work would be involved in formalizing an agreement to commit the third-party to a fixed price. But as noted above, originators today have to have a working knowledge of third-party settlement service prices to fill out a GFE. Therefore, it is only the increase in burden that would need to be accounted for here.

It is difficult to estimate these incremental costs. But to provide an order of magnitude, it is estimated that it takes an average of 10 additional minutes per loan for the originator to arrange the pricing that protects the originator from the costs of the tolerances being exceeded.[75] For a brokerage firm originating 250 loans per year, 10 minutes per loan would come to 42 hours or about

[73] Upfront mortgage insurance is not included in the overall 10% tolerance. It has a zero tolerance because upfront private mortgage insurance charges (which are rare) along with upfront FHA and VA insurance charges are well known.

[74] Other originators may rely on vendor management companies (or vendor management departments within their own company) for pricing information about third-party services.

[75] These 10 minutes would be beyond what the originator spends today to seek out good choices for his borrowers.

one week's worth of one employee's time per year. Thus, this seems to be a reasonable starting point for estimation. For the estimated 12,500,000 loans, that comes to 125,000,000 minutes or 2,083,333 hours. At $72 per hour, this comes to a total of $150 million for all firms and $78 million for small firms. If it takes 20 extra minutes per loan instead of 10, these costs come to $300 million and $156 million respectively and would be two weeks of one employee's time per year for a brokerage firm making 250 loans per year. Table A–9 details the distribution of these costs among the retail mortgage originating industries. With a larger number of loans (15,500,000), total costs are $186 million for all firms (at ten minutes per loan) and $97 million for small firms.

TABLE A–9.—INCREMENTAL COSTS OF THIRD-PARTY PRICING ARRANGEMENTS FOR THE NEW GFE

Industry	Total third-party pricing arrangement cost	Small business cost
Mortgage Brokers	$180,000,000	$126,000,000
Commercial Banks	49,275,600	9,357,436
Thrifts	23,394,000	2,882,141
Mortgage Banks	37,236,000	15,475,282
Credit Unions	10,094,400	2,941,508
TOTAL	300,000,000	156,656,367

One wholesale lender, ABN–AMRO, offers a One-fee program to brokers. In it, the borrower gets a fixed price for many services, including many third-party services. Under the new GFE, arrangements like this would solve the broker's tolerance compliance requirements with the wholesaler making the arrangements for many of the third-party services and negotiating the prices for them. So it may be that (mostly large) wholesalers offer (mostly small) brokers a lower cost alternative to complying with the tolerance requirements of the new rule. If so, then the small business burden above would be an overestimate. Vendor management companies are increasingly appearing in the market, not only providing third-party pricing information, but also offering monitoring and quality control services for originators.

Appendix VII.F. Efficiencies and Reductions in Regulatory and Compliance Burden: The New GFE

Efficiencies come from time saved by both borrowers and originators as a result of forms that are easier to use, competitive impacts in the market, the decrease in the profitability of searching for victims, and the decrease in discouraged potential homeowners. All these are ongoing as opposed to one-time costs.

Appendix VII.F.1. Shopping Time Saved by Borrowers

It should be noted that the increased burden on originators of arranging third-party settlement services is likely to be much more than offset by a reduction in the aggregate shopping burden for third-party providers incurred by borrowers. Originators will be highly motivated to find low third-party prices. Originators could pass the savings on and make it easier to appeal to borrowers, or alternatively, could raise their origination fee by the savings in third-party fees and earn more profit per loan. Or the final result could fall somewhere in between the two. Regardless of which path any originator chooses, the lower third-party prices work to his or her advantage; originators will probably be aggressive in seeking out lower prices. The borrower benefits to the extent that, upon receipt of the GFE, he or she immediately has good pricing information on third-party services. The borrower could immediately decide to use the originator's third parties, in which case his or her search is over. Or, the borrower could search further with the originator's prices as a good starting point and available as a fall-back, in which case the borrower's search efforts are likely to be greatly reduced. In both cases the borrower searches less.

Considering the number of loans the average originator closes per year, the aggregate decrease in search efforts by borrowers is very likely to exceed the increase in aggregate search effort by the originators. For example, if each borrower saves an average of 15 minutes in shopping for third-party services, then the total savings to borrowers would be $234 million.[76] As discussed Sections VII.E.1 and VII.E.2 on tolerances, the new form and the tolerances will enable borrowers to save time shopping for loans and for third-party settlement service providers. If the new forms save the average applicant one hour in evaluating offers and asking originators follow-up questions, borrowers save $935 million.[77] The total value of borrower time saved shopping for a loan and third-party services comes to $1,169 million.

Appendix VII.F.2. Time Saved by Originators and Third-Party Service Providers

Originators and third-party settlement service providers will save time as well. If half the borrower time saved in (1) above comes from less time spent with originators and third-party settlement service providers, then originators spend half an hour less per loan originated answering borrowers' follow-up questions and third-party settlement service providers spend 7.5 minutes less with borrowers for a saving of $765 million[78] and $191 million, respectively, for a total of $956 million.

Appendix VII.F.3. Average Cost Pricing

As discussed in Chapter 3, the proposed rule allows average cost pricing. This reduces costs because firms do not have to keep up with an itemized, customized cost accounting for each borrower. This not only saves costs when generating the GFE, it also saves quality control and other costs afterward. Industry sources have told HUD that this could be a significant cost savings under packaging.

Appendix VII.F.4 Time Saved From Average Cost Pricing

As explained above, there will be reductions in compliance costs from average cost pricing. It is estimated that the benefits of average cost pricing (e.g., reduction in the number of fees whose reported values must be those specifically incurred in each transaction) will lead to a reduction in originator costs of 0.5 percent, or $210 million. No breakdown of fees is needed. No knowledge of an exact fee for each specific service needed for the loan is required for the GFE. In addition, no exact figure for the amount actually paid needs to be recorded for each loan and transmitted to the settlement agent for recording on the HUD–1. The originator only needs to know his or her approximate average cost when coming up with a package price that is acceptable. The cost of tracking the details for each item for each loan is gone.

Appendix VII.F.5. Other Efficiencies

Chapter 3 discusses additional efficiencies of the new GFE. The lower profitability of seeking out vulnerable borrowers for non-competitive and abusive loans should lead to a reduction in this activity. If the decline in

[76] Calculated as follows: 21,250,000 projected mortgage applications (see Chapter 2) times $44 per hour times 0.25 hour (or 15 minutes) gives $233.750 million. The $44 per hour figure is based on the average income ($92,000) of mortgage borrowers, as reported by HMDA; the $92,000 income figure is divided by 2,080 hours to arrive at the hourly rate of $44.23 or $44. If the borrower saved 30 minutes in shopping time, then the total savings would be $330 million.

[77] Calculated as follows: 12,500,000 loans times 1.7 applications per loan times 1 hour per application times $44 per hour, the average hourly income of loan applicants ($92,000 per year/2080 hours per year). See earlier footnote.

[78] Calculated as follows: 12,500,000 loans times 1.7 applications per loan times 0.5 hours per application times $72 per hour, the average hourly income of loan originators ($150,000 per year/2,080 hours per year).

this activity represented one percent of current originator effort, this would result in $420 million in savings to firms (see Section VII.B of Chapter 3 of the RIA).

There are other potential efficiencies that are anticipated from the new GFE approach but would be difficult to estimate. For example, studies indicate that one impediment to low-income and minority homeownership may be uncertainty and fear about the home buying and lending process. The new GFE approach should increase the certainty of the lending process and, over time, should reduce the fears and uncertainties expressed by low-income and minority families about purchasing a home (see Section VII.F of Chapter 3). As discussed in Section IV.D.4 of Chapter 2, improvements in lender information (e.g., interest and settlement costs) should also lend to a general increase in consumer satisfaction with the process of taking out a mortgage (see CFI Group, 2003).

Appendix VIII. Costs Associated With Changes to the HUD–1 and the Closing Script

This section discusses costs on closing agents associated with the new HUD–1 and the required closing script. Section VIII.A explains the data and VIII.B the analysis of costs.

Appendix VIII.A. Data on Settlement Service Providers

Section VII.A reproduced background data on the retail mortgage origination industries. Since the GFE affects settlement service providers as well as retail mortgage originators, this section recapitulates data from Chapter 5 of the RIA on the settlement services industries. Readers are referred to Section IV of Chapter 5 for a more detailed treatment of the data.

Table A–10 provides the total number of firms, the number of small employer firms, the number of nonemployer firms, and the percent of small firms (employer and nonemployer) in industries that provide settlement services (see Chapter 5 for details on the classification of small employer firms in these industries). These constitute all of the firms in these industries in 2004, according to the Census Bureau. As discussed below, for Offices of Lawyers, Other Activities Related to Real Estate (Escrow), Surveying & Mapping Services, Extermination & Pest Control Services, and Credit Bureaus, the figures in Table A–10 almost certainly overstate the number of firms actually participating in residential real estate settlements.[79]

TABLE A–10.—FIRMS IN INDUSTRIES PROVIDING SETTLEMENT SERVICES

Industry	Total firms	Small employer firms	Nonemployer firms	Percent small firms
Direct Title Insurance Carriers	2,094	1,865	135	95.5%
Title Abstract and Settlement Offices	14,211	7,889	6,203	99.2
Offices of Lawyers	401,553	165,127	234,849	99.6
Other Activities Related to Real Estate (Escrow)	463,545	15,119	448,409	99.996
Offices of Real Estate Appraisers	65,491	15,656	49,802	99.9
Surveying & Mapping Services	18,224	8,990	9,196	99.8
Extermination & Pest Control Services	18,000	10,018	7,935	99.7
Credit Bureaus	1,285	710	545	97.7
Total	984,403	225,374	757,074	99.8

Source: Census Bureau.

Table A–11 provides the total number of employees in employer firms, and the number and percent of employees in small employer firms for each of the settlement services industries.[80] The Census Bureau does not count owners of employer and non-employer firms as employees. The number of ''workers'' in these industries is understated by the number of employees as defined by the Census Bureau because in a nonemployer firm the owner is a production worker as is likely also true for the owner of a small employer firm. Using the Census Bureau's count of employees for computing the compliance burden of a rule may tend to understate the burden.[81] Thus in computing the number of workers in these industries, one worker is added for each small employer firm and each nonemployer firm to the total number of employees (see Table A–13 below for these results).

TABLE A–11.—EMPLOYEES IN INDUSTRIES PROVIDING SETTLEMENT SERVICES

Industry	Total employees in employer firms	Employees in small employer firms	Percent employed by small firms
Direct Title Insurance Carriers	75,702	7,144	9.4%
Title Abstract and Settlement Offices	79,819	47,913	60.0
Offices of Lawyers	1,122,723	657,749	58.6
Other Activities Related to Real Estate (Escrow)	67,274	40,074	59.6
Offices of Real Estate Appraisers	45,021	37,300	82.8
Surveying & Mapping Services	61,623	53,610	87.0
Extermination & Pest Control Services	95,437	55,565	58.2
Credit Bureaus	25,555	5,135	20.1

[79] As shown by the fourth column, practically all firms qualify as small businesses. This is partially due to the large number of non-employer firms (which automatically qualify as a small business) included in the Bureau of Census data. See Chapter 5 for further discussion of this issue and for small business percentages for employer firms only. Also note that while the number of firms is drawn from year 2004 data, the small business percentages are based on 2002 data from the Bureau of Census; while they are estimates, they are probably highly accurate ones. Also see Chapter 5 for the source of the small business percentages and for alternative, year-2002-based small business percentages based on firms with less than 100 employees.

[80] The ''Total Employees'' data in Table A–11 are for the year 2004. The ''Employees in Small Employer Firms'' data are obtained by multiplying the total employee data for 2004 by the percentage of employees in SBA-defined small firms obtained from 2002 Bureau of Census data; thus, the small employee data are estimates but probably highly accurate ones. See Chapter 5 for discussion of the 2002 small business percentages.

[81] For example, if worker training were required by the rule, and burden estimates were based on Census Bureau employee statistics, the compliance burden for nonemployer firms would be estimated at zero, while clearly at least one ''worker,'' the owner, would require the training.

TABLE A–11.—EMPLOYEES IN INDUSTRIES PROVIDING SETTLEMENT SERVICES—Continued

Industry	Total employees in employer firms	Employees in small employer firms	Percent employed by small firms
Total	1,573,154	904,490	57.5

Source: Census Bureau (note: non-employer firms not included).

Table A–12 provides information on the volume of settlements for various industries that participate in the settlement process and the number and percent handled by small firms within each industry.[82] Note that while the distribution among Direct Title Insurance Carriers, Title Abstract and Settlement Offices, Offices of Lawyers, Lawyers and Escrow, Offices of Real Estate Appraisers, and Credit Bureaus is based on all settlements, the numbers and percentages for the other industries (Surveying & Mapping Services and Extermination & Pest Control Services) represent the proportion of settlements in which they are involved.[83] The allocation is based upon estimated dollar revenues from settlements for these industries.[84] Totals are estimated based on the number of mortgage originations, 12,500,000 that would occur in a ''normal'' year of mortgage originations (i.e., not in a year with a refinancing boom).

TABLE A–12.—VOLUME OF SETTLEMENT SERVICE ACTIVITY

Industry	All settlements	Percent of settlements	Settlements by small firms	Percent industry settlements by small firms
Direct Title Insurance Carriers	5,375,000	43.00%	258,000	4.80%
Title Abstract and Settlement Offices	4,749,953	38.00	2,365,476	49.80
Lawyers and Escrow	2,375,048	19.00	2,137,543	90.00
Total Settlements	12,500,000	100.00	4,761,019	38.09
Offices of Real Estate Appraisers	12,500,000	100.00	10,387,500	83.10
Surveying & Mapping Services	3,600,000	28.80	2,926,800	81.30
Extermination & Pest Control Services	5,500,000	44.00	2,964,500	53.90
Credit Bureaus	12,500,000	100.00	1,312,500	10.50

A larger volume of mortgage activity can also be examined, for example, to reflect a ''refinance environment''.[85] In this case, the volume of settlement activity would be distributed as follows: 6,665,000 for Direct Title Insurance Carriers, 5,889,941 for Title Abstract and Settlement Offices, 2,945,059 for Lawyers and Escrow, 4,464,000 for Surveying & Mapping Services, 6,820,000 for Extermination & Pest Control Services, and 15,500,000 for both Offices of Real Estate Appraisers and Credit Bureaus.[86]

The employee figures reported in Table A–11 misstate the number of workers actually participating in residential real estate settlements. This section offers some estimates of that figure, although it is recognized that they are subject to some uncertainty given the limited information that is available. Table A–13 provides one estimate of the total number of workers and the number and percent of workers in small firms engaged in performing settlements by industry. For Title Abstract and Settlement Offices and the combined Lawyers and Escrow industry, it is based on the volumes of settlement activity depicted in Table A–12

[82] The small business percentages in Table A–12 are the shares of revenue accounted for by small business, as reported and explained in Chapter 5—in other words, the small business share of revenues is being used here as a proxy for the small business share of settlements (or mortgage loans). There are two other points that should be made about these data. (1) Figures for Offices of Lawyers and Other Activities Related to Real Estate (Escrow) are combined into the new ''Lawyers and Escrow'' category. This is because there is insufficient information to allocate volumes of settlements between these two industries (see Section IV.B.5 of Chapter 5 for further explanation). As explained in Chapter 5, the small business revenue share for the combined ''Lawyers and Escrow'' category is raised to 90% (versus 47.8% for all lawyers and 86.9% for escrow firms based on 2002 Census Bureau revenue data) under the assumption that lawyer and escrow firms engaged in real estate activity are likely to be the smaller firms operating in these industries. Note that in Table A–13 below, the 90% figure is also used for the share of employees in small firms in this combined industry. (2) As explained in Section IV.B.4 of Chapter 5, there are probably no small businesses in the Direct Title Insurance Carriers (DTIC) industry, which includes the large title insurance firms. The 4.8% figure in Table A–12 (as well as the 9.4% figure in Table A–11) is reported to remain consistent with the Bureau of Census data—including it or excluding it does not affect the results in any significant way.

[83] See Step (9) in VII.E.1 of Chapter 3 for the calculation of the proportion of settlements for Surveying & Mapping Services and Extermination & Pest Control Services. Because of their relatively small shares of the overall mortgage business, different shares for these industries would not materially affect the overall small business shares of revenue. While it is recognized that the other industries may not be involved in every mortgage origination and settlement transactions (e.g., an appraisal may not be required for some mortgage originations), they are certainly involved in most such transactions and, therefore, it is assumed here that they are involved in all transactions.

[84] As explained in Chapter 5, there is also some uncertainty about the distribution of mortgage-related business and revenues among the various title-related industries. Table A–12 assumes the following distribution: Direct Title Insurance Carriers (43.0%), Title Abstract and Settlement Offices (38.0%), and Lawyer and Escrow (19.0%). Section IV.B.5 of Chapter 5 considers other distributions and suggests the following ranges for the specific industry shares: Direct Title Insurance Carriers (35%–50%), Title Abstract and Settlement Offices (29%–43%), and Lawyer and Escrow (17%–29%). Given limited available information, it is difficult to determine a precise estimate, which is why Chapter 5 includes several sensitivity analyses. But obviously, reducing the relative weight of the DTIC or increasing the relative weight of the lawyer-escrow industry would increase the small business share of settlements. Readers are referred to Section IV of Chapter 5 for a more complete analysis of the relative importance of each title-related industry, particularly as it affects the overall small business percentage for title- and settlement-related work.

[85] In the projection given in the text, home purchase loans were assumed to stay the same (7.5 million, or 60% of the 12.5 million in mortgages), while refinances increased from 5 million (or 40% of the 12.5 million mortgages) to 8 million of the 15.5 million total (home purchases remain at 7.5 million).

[86] The settlement volume for small businesses during a high volume year can be obtained using the small business percentages from Table A–12, giving: 319,920 for Direct Title Insurance Carriers, 2,933,191 for Title Abstract and Settlement Offices, 2,650,553 for Lawyers and Escrow, 3,629,232 for Surveying & Mapping Services, 3,675,980 for Extermination & Pest Control Services, 12,880,500 for Offices of Real Estate Appraisers, and 1,627,500 for Credit Bureaus.

and the productivity level of Title Abstract and Settlement Offices (i.e., settlements per worker).

The figure for total workers in Title Abstract and Settlement Offices is the sum of: all employees (79,819), small firms (7,889), and nonemployer firms (6,203), or 93,911. (Small firms and nonemployer firms are added to count the owners of those firms as production workers as discussed in the description of Table A–11 above). The corresponding figure for workers in small firms is the sum of: Employees of small firms (47,913), small firms (7,889), and nonemployer firms (6,203), or 62,005 workers (representing 66% of all workers in Title Abstract and Settlement Offices). These figures are reported in Table A–13 below. In this industry, there are 50.6 settlements per worker (obtained by dividing the 4,749,953 settlements from Table A–12 by the 93,911 workers).[87]

In the combined Lawyers and Escrow industry group, worker productivity is assumed to be half of that in Title Abstract and Settlement Offices on the grounds that these workers may not do settlements full time and because of the general lack of information on the degree of settlement activity in these broadly defined industries. Thus, the number of workers in this category (93,914) is computed by dividing the number of settlements handled by the industry from Table A–12 divided by one-half the settlements per worker in the Title Abstract and Settlement Offices industry.

For Direct Title Insurance Carriers, many workers are not engaged in actual settlements, but rather in the title insurance function itself. Direct Title Insurance Carriers provide title insurance through agents as well as both direct sales of title insurance and associated settlement services to consumers through branch offices. They also, of course, perform the title insurance function itself. HUD examined the annual reports of the large direct title insurance carrier companies to attempt to estimate the proportion of employees of these companies engaged in providing settlement services. It is estimated that approximately 70 percent of workers in this industry, or 54,391 workers, are engaged in providing settlement services. (See Table A–13).[88]

TABLE A–13.—WORKERS ENGAGED PERFORMING SETTLEMENTS

Industry	Total workers	Workers in small firms	Percent of workers in small firms
Direct Title Insurance Carriers	54,391	6,401	11.77%
Title Abstract and Settlement Offices	93,911	62,005	66.03
Lawyers and Escrow	93,914	84,523	90.00
Total	242,217	152,929	63.14

The estimated numbers of title and settlement workers would be larger under market conditions producing a larger volume of mortgage activity. The estimated distribution of settlements when overall mortgage volume is 115,500,000 was given earlier. To adjust the worker estimates in Table A–13 to reflect the higher mortgage volume requires information about the increase in productivity (i.e., loans per worker) during the higher volume (or heavy refinance) environment. It is not correct to simply adjust the number of workers up by the percentage increase in mortgage loans because the number of loans per worker increases during refinance booms. The earlier analysis of brokers and lenders provided estimates of additional workers in a higher volume market. That analysis was based heavily on trend data through 2002 for the number of workers in the broker industry, as reported by David Olson and his firm, Wholesale Access. The number of loans per broker increased between low and high volume years. Similar trend data do not exist showing the number of title and settlement workers during recent refinance booms. Thus, any adjustment would be somewhat speculative. But it is also important to emphasize that workers hired during high-volume years, for example, are more likely to be temporary or part-time workers. Temporary workers will likely rely on permanent workers for training or information about new rules and regulations. Thus, the numbers in Table A–13 providing estimates of workers in the title and settlement industry serve as a reasonable basis for analyzing the effects of the new regulation among the various settlement and title industries, recognizing that the numbers could vary somewhat depending on the volume of mortgages considered in the analysis.

Estimates of the number of single-family-mortgage-related workers in Surveying & Mapping Services, Extermination & Pest Control Services, and Credit Bureaus are not included because there are insufficient data upon which to base an estimate. Mortgage-related work accounts for a relatively small portion of the overall activity of these industries, and information is not available to separate single-family-mortgage-related business from other activity. In addition, data on workers for these industries are not needed for the analysis of cost savings below. While this information is also not needed below for the appraisal industry, it is possible to produce reasonable estimates of workers for this industry because single-family-mortgage-related work likely accounts for most of the activity in this industry. Using the methodology described above (adding employees of employer firms, non-employer firms, and owners of small firms to arrive at the number of workers), the appraisal industry in the projection year would include 110,479 workers, and 102,758 of these work

[87] There are two caveats with this estimate. First, the estimate depends on the number of settlements in the Title Abstract and Settlement industry, which, as discussed in an earlier footnote, could differ from the number reported in Table A–12 (see Section IV.B.5 of Chapter 5 as well as the earlier footnote for possible ranges of estimates). Second, not all workers in the Title Abstract and Settlement industry are engaged in single-family real estate transactions, which means that the number of workers is overstated and therefore the number of settlements per worker is understated. (Unfortunately, there is no information on the proportion of Title and Abstract workers engaged in single-family mortgage activity, although it is likely that most are.) If the number of settlements per worker is too low, the projection will overstate the number of workers needed.

[88] In 2004, the DTIC industry employed 77,702 workers (based on the definition of worker used in the text). HUD estimates that approximately 70 percent, or 54,391, are engaged in providing settlement services. HUD computed an estimate of the proportion of salaries that large title insurance companies paid to workers engaged in settlement services as follows: (1) The amount of revenue required to carry out the insurance function for policies written by agents was computed as the difference between agent-generated revenue and agent commissions (or agent retention expenses); (2) two percentages were then calculated, (a) the percentage of agent-generated revenue required for the insurance function in agent-written policies as (1) divided by total agent-generated revenue, (b) the percent of all insurance revenue required for the insurance function for agent-written policies as (1) divided by total insurance revenue; (3) the salaries for employees providing the insurance function for agent-written policies was computed by multiplying (2)(b) by total salary expenses; (4) the total salaries for employees engaged in direct sales of insurance (including other settlement services) and providing the insurance function for direct-sales policies was computed by subtracting (3) from total salary expenses; (5) the salaries of employees providing the insurance function for direct-sales policies was computed by multiplying (2)(a) by (4); (6) the salaries of employees selling title insurance directly (and providing other settlement services) was computed by subtracting (5) from (4); finally (7) the percent of salaries paid to employees selling title insurance directly (and providing other settlement services) was computed by dividing (6) by total salary expenses. This analysis was carried out using 2005 data from the annual reports of four title insurance companies (First America, Land America, Fidelity National, and Stewart). The percentage computed in (7) ranged from 67.7 percent to 72.8 percent. Based on these results, HUD assumes that 70 percent of DTIC workers are engaged in providing direct title insurance sales and other settlement services.

in small firms.[89] While some of these appraisers focus on multifamily and commercial properties and/or conduct appraisals for local governments (e.g., estimating the value of properties for tax purposes), most are likely involved in single-family mortgage-related activities.[90]

Appendix VIII.A. One-Time Costs of the New HUD–1 and Closing Script Addendum

Appendix VIII.A.1 Introduction

The proposed HUD–1 is simpler than the existing HUD–1. Nevertheless, there will be change in the form, including the introduction of the closing script addendum, and the settlement industry will need to learn how the proposed form works. The primary focus will be on how to put the numbers in the right place. The service charge and the charge or credit for the interest rate chosen will be placed outside the columns in the HUD–1 while the adjusted origination charge will be in the columns, borrower or seller, or listed as POC. This is to avoid double counting that the settlement agent would certainly want to avoid in order that would lead to erroneous totals. For third-party fees selected by the lender located in section 3 of the proposed GFE, the individual entries rather than the subtotals will be entered in the columns or as POCs and the subtotals will not be reported as such. The same is true of the third-party fees selected by the borrower located in section 5 of the proposed GFE. The individual entries are entered because they can wind up in different series of the HUD–1 and subtotals would be difficult to reconcile. The rest of the proposed GFE fees go in the columns or as POCs. The settlement agent must be aware for each GFE item listed on the HUD–1 that totals from the HUD–1 must include figures from both the borrower column and the seller column, as well as any figure listed as POC.

The required script will represent a more significant change for the industry than the new HUD–1. Although some training may be required, it is not likely to be substantial since settlement agents are already very familiar with what information to provide at a closing. The script simply standardizes the explanation of the loan terms and any differences between the settlement charges on the GFE and HUD–1. The burden of the script is more likely to be felt on software developers.

The costs can be categorized similarly as for the new GFE: Software costs (including training), legal consultation costs, and training costs. The total one-time compliance cost to the industry is $169 million, of which $110 million is borne by small business.

Appendix VIII.A.2 Software Costs

Developers of settlement software and settlement agents will be subject to software costs. They will face the following two changes: A reorganization of the HUD–1 form and the requirement of a closing script explaining the crosswalk between the GFE and the final HUD–1. The changes to the HUD–1 form would not require much work from programmers. The only programming to be done is changing the manner in which information is displayed on the HUD–1 form. First, there will be fewer fees. Second, references to the corresponding figures in the GFE would need to be inserted by the software developers.

Including the script would require more effort because it is a completely new form. The programming itself would not be challenging since the script only contrasts data from the HUD–1 and the GFE and shows whether the tolerances are met. The more complex calculations concerning the loan terms are not required to be done by the settlement agent but by the lender. Indeed, it is possible that some producers of loan origination software will begin to feature a crosswalk application that generates an almost complete script for the settlement agents to finish. Settlement agents may prefer to put together the script themselves. There would be a strong demand for settlement script software given the importance of the script as a means to double check the final figures. Software would perform the important task of calculating the difference between the figures on the initial GFE and the actual settlement costs and then check whether they are within the tolerances.

We will assume that the costs of software updates and software training are the same as for the new GFE. Given the number of workers and the distribution by firm size, the total cost of new software is $62 million, of which $46 million is borne by small business. The cost of the changes to software is $14 million (of which $11 million is borne by small business) and the opportunity cost of the time spent learning the new software is $48 million (of which $34 million is borne by small business).

Appendix VIII.A.3. Legal Consultation Costs

Legal consultation will be less involved for the HUD–1 form and the script than for the new GFE. The only issue that is important for the settlement industry to understand is that practicing discounting as well as volume-based discounting is permitted. However, settlement firms may require additional legal consultation to be on the safe side. We make the same assumptions as for the GFE: All firms purchase a minimum of two hours of legal consultation at a cost of $200 an hour and that additional legal service are demanded on the basis of the volume of business. We estimate that the total legal costs to the settlement industry will be $37 million of which $18 million is borne by small business. The cost of legal fees is lower for the HUD–1 form than for the GFE because there are less firms involved in settlement than in mortgage origination.

Appendix VIII.A.4. Training Costs

Workers who perform settlements will only need to learn how to fill out the simplified HUD–1 form and the closing script. The quantities are provided to settlement agents by the GFE, so training will be much less involved. Assuming four hours of training at an opportunity cost of $72.12 per hour (based on a $150,000 fully-loaded annual salary); tuition of $250 per worker for small firms and a discounted tuition of $125 per worker for large firms; and that half of the workers in small firms and one quarter of the workers in large firms require training; then the total cost of training is $71 million, of which $62 million is borne by small business.

Appendix VIII.B. Recurring Costs of the New HUD–1 and the Closing Script Addendum

There are no increased recurring costs associated with the proposed HUD–1. The proposed HUD–1 will very likely have fewer entries than the existing HUD–1 which will require fewer explanations of figures than is true with the existing forms. This is because of the combined subtotals presented in many sections in the proposed GFE in lieu of the frequently numerous broken out individual fees that we see on the GFE. The same is true when comparing the proposed HUD–1 to the existing HUD–1. Comparing the proposed GFE to the Proposed HUD–1 should be simpler than in the past because it will be much easier to find entries on the proposed HUD–1 that correspond to the proposed GFE because they have the exact same description. And, of course, there are fewer entries to deal with. It is hard to imagine how simpler forms could be more costly to explain to borrowers.

There will be recurring costs from the HUD–1 addendum. The closing script will serve the purpose of a crosswalk between the HUD–1 form and page 2 of the GFE. Requiring the script would standardize the explanation of the HUD–1 form. One could reasonably assume that the script would impose no additional burden on the typical conscientious settlement agent. Although there is currently no standard procedure for a settlement, most settlement agents are conscientious so that reviewing the terms of the loan and settlement costs with the borrower is standard practice. In the occasional case of the hasty or careless settlement agent today, the borrower is likely to ask for an explanation of the correspondence between the GFE form (issued at the time of shopping) and the HUD–1 form (issued at closing). However, a detailed description of the loan and closing costs is not compulsory. Requiring that a script be read will impose a cost on those settlement agents who do not automatically explain all costs of the loan at closing. Thus, rather than assuming that a script would be neutral in its impact on the settlement industry, we will account for the possibility of positive compliance costs.

[89] The total number of workers is derived as follows: 45,021 employees in employer firms (from Table A–11) plus 49,802 non-employer firms (from Table A–10) plus 15,656 owners of small firms (from Table A–10), which yield 110,479 workers. The number of workers in small businesses is derived as follows: 37,300 employees in small employer firms (from Table A–11) plus 49,802 non-employer firms (from Table A–10) plus 15,656 owners of small firms (from Table A–10), which yields 102,758 workers in small businesses.

[90] One would think that practically all of the owners of the 49,802 non-employed firms appraised single-family properties, as well as most of the 37,300 employees in small employer firms. One could argue that the number of workers for the entire industry in 2004 is a upper bound since mortgage activity in that year was higher than in the projection year. Additionally, automated valuation models (AVMs) may have reduced the demand for appraisers; particularly on refinance loans (see Section V.A of Chapter 5 for a discussion of AVMs).

A mandatory script could impose a cost on a settlement agent by increasing the time required to perform a settlement. A cost will arise only when a scripted settlement takes longer than the current unscripted one. First, agents would be obliged to complete the script, which would consist of collecting the data (approximately twenty on the loan terms, depending on the loan and a comparison of approximately fifteen settlement charges from both the GFE and HUD–1), fill in the blanks on the script, determine the tolerances for the fees, and check that the figures on the HUD–1 are within the tolerances of those from the GFE. An experienced settlement agent who is organized might be able to do this work in fifteen minutes. Even inexperienced agents would not need to spend much time when assisted by software. There may be the occasional loan, which is especially difficult because the loan terms are complex and because the settlement agent would like to double-check the complicated calculations made by the lender. Such loans may require thirty minutes to complete the script. We will assume the worst case scenario and that preparing a script requires thirty more minutes on average than if there were no script. Second, reading the script would take five minutes longer on average than if there were no formal procedures for explaining the HUD–1 form. For the agent who currently reviews the HUD–1 form with the borrower requiring a review will not constitute an additional burden. Third, we assume that the net effect on time spent discussing borrowers' questions is an additional ten minutes for the average loan.[91] The script may induce questions on some issues but it is also expected that a methodical explanation will obviate the need for others. For simple loans, the net effect is expected to be nil. In the case of more complex loans, clarifying the terms of the loan is expected to add from five to ten minutes. We use an average of ten minutes across all loans.

In total, the script could lead to an additional forty-five minutes spent on the average settlement. The opportunity cost of that time to the settlement firm would be $54 ($72 per hour, which is derived from a $150,000 fully loaded salary). The total cost of the script in a normal year (12.5 million originations) would be $676 million and $838 million in a high volume year (15.5 million originations).[92] We assume that 38.1 percent of the closings are done by small business (see Table A–12) so that the recurring cost on small business would be $258 million in a normal year and $319 million in a high volume year. It is possible that the time added by the script is an overestimate. If the required script led to an additional thirty minutes spent on a settlement (twenty minutes preparing the script, five minutes reading it, and five minutes answering questions), then it would cost the industry $36 per closing, totaling $451 million in a normal year and $559 million in a high volume year.

We do not include the additional ten minutes spent by the borrower at the settlement as a cost to the borrower because it is expected that the script is more likely to reduce the time spent by the borrower trying to determine whether the fees of their HUD–1s (issued at time of shopping) were in accord with the fees on the GFE and the tolerances. In addition, a borrower may be less likely to ask to be accompanied by someone to help them translate the crosswalk. Indeed, it is possible that the extra time spent by settlement agents is more than outweighed by the time saved by borrowers.

The benefits of the script are not estimated separately from the benefits of the new GFE ($6.48–$8.38 billion, see Section I.B of Chapter 3). It is assumed that the script reinforces the consumer savings of the new GFE by compelling settlement agents and borrower to check the compliance with the tolerances. The script is a vital part of the new GFE. Requiring is expected to increase the number of consumers who realize the full benefits of the proposed rule.[93] The benefit of the script is to double-check the final figures.

Appendix IX References

America's Community Bankers. 2002. Comments from America's Community Bankers regarding ''Proposed Rule on Real Estate Settlement Procedures Act (RESPA); Simplifying and Improving the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers, Docket No. FR–4727–P–01; 67 FR 49134–49174 (July 29, 2002),'' October 28, 2002.

Consumer Mortgage Coalition to United States Senate. Hearing on the Impact of the Proposed Real Estate Settlement Procedures Act Rule on Small Business and Consumers. Committee on Banking. (18 April 2003).

Jackson, Howell E., and Jeremy Berry. 2002. ''Kickbacks or Compensation: The Case of Yield Spread Premiums.'' Unpublished Paper, pp. 1–52.

Mortgage Bankers Association of America. 2003. ''RESPA Interest Rate Working Group Report.'' Comments regarding ''Proposed Rule on Real Estate Settlement Procedures Act (RESPA); Simplifying and Improving the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers, Docket No. FR–4727–P–01; 67 FR 49134–49174 (July 29, 2002),'' October 28, 2002.

Sadow, Eric S. 2002. Comments from the Associate General Counsel, Bank of America Corporation regarding ''Proposed Rule on Real Estate Settlement Procedures Act (RESPA); Simplifying and Improving the Process of Obtaining Mortgages to Reduce Settlement Costs to Consumers, Docket No. FR–4727–P–01; 67 FR 49134–49174 (July 29, 2002),'' October 25, 2002.

Urban Institute. Descriptive Analysis of FHA Loan Closing Costs, Prepared for Department of Housing and Urban Development for internal use only by Signe-Mary McKernan, Doug Wissoker, and William Margrabe. May 9, 2007a.

Urban Institute. A Study of Closing Costs for FHA Mortgages, Prepared for Department of Housing and Urban Development Office of Policy Development and Research by Susan Woodward. November 29, 2007b.

[FR Doc. 08–1015 Filed 3–13–08; 8:45 am]

BILLING CODE 4210–67–P

---

[91] Although it is not appropriate to count this additional time answering questions as a burden for the Paperwork Reduction Act because conveying this information is a standard business practice, it is counted as a potential cost in the Economic Analysis because the additional time that settlement agents may need to spend answering questions generated by the script will reduce the time that settlement agents could spend doing something else.

[92] As for the GFE, an alternative method could be used to generate an estimate of the opportunity cost of time spent on a script. Instead of assuming a $72.12 opportunity cost (from a $150,000 fully-loaded salary), one could construct a cost estimate from industry-specific data. For example in Tucson, Arizona, the cost of labor (compensation and benefits) of a Real Estate Clerk is $16.66 per hour and $74.61 per hour for a Real Estate Attorney. If the Real Estate Clerk spends an additional twenty-five minutes preparing for a settlement due to the script and the Real Estate Attorney spends an additional twenty minutes reading and reviewing the script; and if we include office rent at 34 cents a minute and computer equipment at 7 cents a minute both for forty-five minutes, then the burden of the script would be $32.12 per closing or a total $401 million in a normal year or $497 million in a high-volume year.

[93] Given our estimated compliance cost, the benefits of the script ($518–$670 per loan) would outweigh the costs as long as the absence of a standardized script would decrease the probability of realizing those consumer benefits by a few percentage points (8.1 for our higher estimate of the benefits and 10.4 for the more conservative estimate).